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In The

Supreme Court of the United States

October Term, 1997

DAVID W. SILVERMAN, as Independent Fiduciary of The Unitron Graphics, Inc. Profit Sharing Trust and Unitron Graphics, Inc. Profit Sharing Trust-Union and Non-Union Division,

Petitioner,

vs.

MUTUAL BENEFIT LIFE INSURANCE COMPANY, PRINCIPAL MUTUAL LIFE INSURANCE COMPANY and HELENE GORNY,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

AS TO MUTUAL BENEFIT LIFE INSURANCE COMPANY

1. Whether the Second Circuit erred when it allowed individual account plans[1] funded by participants' salary reductions to be liquidated and transferred to one of the plan sponsor's designated trustees without the participants' knowledge or approval.

2. Whether the Second Circuit erred when it exculpated from liability an investment fiduciary insurance company which, without making any inquiry into the legitimacy of a non-investment trustee's directions or inquiry of the plan sponsor, or providing notification to the participants affected, liquidated the investments in designated individual accounts and forwarded the cash proceeds to the control of a non-investment trustee.

3. Whether the Second Circuit erred in dismissing claims of loss by embezzlement from participants' separate retirement accounts by its holding that an insurance company, which makes available to participants diverse investment options for individual accounts plans, was without liability as

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[1] The terms "individual account" and/or "individual account plan" as used throughout this petition as well as in the courts below refer to those retirement plans which meet the requirements of 26 U.S.C. § 401(k) and § 404(c) of ERISA, 29 U.S.C. § 1104(c).

an investment fiduciary when it followed directions of one of the non-investment trustees appointed by the Plan sponsor.

AS TO PRINCIPAL MUTUAL LIFE INSURANCE COMPANY

4. Whether the Second Circuit erred in finding that no liability attaches to an investment fiduciary insurance company which breaches its fiduciary responsibility by secreting its co-fiduciaries' illegal retention of funds earmarked for participants' retirement accounts (which resulted in criminal embezzlement) unless the participants could affirmatively show that "but for" the secretion and breach of fiduciary duty, recovery could have been made from the co-fiduciary embezzlers.

5. Whether the Second Circuit erred by holding that no liability attaches to an investment fiduciary insurance company pursuant to the Employee Retirement Income Security Act of 1974 ("ERISA") §§ 404 and 405, 29 U.S.C. §§ 1104 and 1105, when such fiduciary purposefully engaged in secretion of facts and failed to notify participants or the Department of Labor of a co-fiduciary's breach but, rather, rendered misleading advice to participants, unless the participants can establish prima facia that a recovery could have been made against that co-fiduciary.

PARTIES TO THE PROCEEDING

Petitioner David W. Silverman, plaintiff-appellant below, was appointed by Order dated November 22, 1994 in a proceeding entitled

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK
----------x
UNITED STATES OF AMERICA

-against- 93 CR 955 (ILG)

JACOB ZUCKER and AARON FERTIG,

Defendants.
----------x

as an independent fiduciary "with plenary authority and control with respect to the management and/or administration of the employee benefit trusts created by Unitron Graphics . . .".

Mutual Benefit Life Insurance Company, Principal Mutual Life Insurance Company, and Helene Gorny were defendants-appellants below.

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PETITION FOR A WRIT OF CERTIORARI

INTRODUCTION

Both Congress and the executive branch, keenly aware that the citizenry is not adequately saving for their ultimate retirement years, have urged increased savings. This June the nation's top political leaders, as well as some 200 government leaders and others, met at the National Saver Summit in Washington. At this conference, a national policy to increase savings by urging citizen employees to make full use of their 401(k) salary reduction plans, was discussed. Of course, by doing so, employees must turn over their hard-earned monies to large private institutions, such as banks and insurance companies. Fear of fraud and embezzlement is an omnipresent danger when pension monies are under the control of any private enterprise. Such large pools of money act as a gravitational point to those intent upon their appropriation, even to those who hold the legal status of a fiduciary.

Within the parameters of a defined benefit plan, the issues of employee contributions and ownership of those contributions are now before this Court in Hughes v. Jacobson, 105 F.3d 1288 (1997) and 128 F.3d 1305 (1997), Cert. Petition No. 97-1287 (granted). Such a determination is equally important to participants of defined contribution retirement accounts created pursuant to 26 U.S.C. §§ 401(k) and 404(c) of ERISA, 29 U.S.C. § 1104(c), where no benefit is promised and all losses, investment and otherwise, are the responsibility of the participant. See Pension Benefit Guaranty Corp. v. LTV Corp., 496 U.S. 634, 637 n. 1 (1990). Should Congress allow self-directed investments as an adjunct to Social

Security, the history of ERISA in determining the ownership of these assets will be critical to the issue of recovery of funds lost due to embezzlement and fraud.

The court below ignored petitioner's contention that the legislative paradigm of individual account plans precludes any person other than the participant from exercising the power to liquidate and transfer the account. Paid investment fiduciaries managing these large pools of money are relieved of responsibility by the decision of the Second Circuit below for their breaches of fiduciary duty in failing to exercise even the slightest duty of inquiry as to the veracity of instructions received by non-investment fiduciaries[2] directed toward the removal of participants' individual accounts. The Second Circuit instructs trustees that freedom from liability flows from a "hear no evil, see no evil, speak no evil"[3] administration of trust funds when

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[2] The term non-investment fiduciary as used throughout this petition, as well as in the courts below, refer to fiduciaries appointed by the plan sponsor and, in this case, to that portion of the Trust Agreement which provided, "Participants may choose among the Investment Accounts defined in the Contract as selected by the Employer, change their choices and transfer between Investment Accounts, as permitted in the Contract. The Participant's choice of Investment Accounts relieves the Trustee(s) of fiduciary responsibility."

[3] Legend related to the "Three Wise Monkeys" carved over door of Sacred Stable, Nikko, Japan, in Bartlett's Familiar Quotations, 919 (Emily Morison Beck ed., 15th ed., 1980). Quoted by Bright, J., dissenting on

the insurance carrier and sponsor have agreed between themselves how they will handle the participants' monies. The clear breach of a duty of inquiry, and thus its fiduciary duty, by Mutual Benefit Life Insurance Company ("Mutual Benefit") was graciously forgiven by the courts below on the theory that following a plan sponsor's appointed trustee's improper direction was a complete defense.

Paid investment fiduciaries managing these large pools of money are likewise relieved of responsibility by the decision herein of the Second Circuit for their complicity in and suppression of a wrongful withholding of participants' monies by co-fiduciaries.

The litany of inaction, suppression of truth, and misstatement of known facts to inquiring participants by Principal Mutual Life Insurance Company ("Principal") is staggering. Having affirmatively heard, seen and spoken evil, Principal's defense in the courts below was sustained; to wit, that unless the participants could establish a prima facie case that recovery could have been made against the embezzling co-fiduciaries, Principal bears no liability. The Second Circuit rejected the participants' arguments that recovery against the embezzling fiduciaries was an issue of damages and not liability, and that the failure to notify the participants or the Department of Labor (the "DOL") of co-fiduciary breaches was a clear, independent breach, casting Principal in liability.

Herman v. Mercantile Bank, 1998 U.S. App. LEXIS 8342, p.8, n.4 (8th Cir. 1998).

If the national goal is for the citizenry to save in their individual accounts as a vehicle to enhance economic freedom upon retirement and, at the same time, to shift fiduciary investment responsibility to the participant, it is a subversion of ERISA's goal to allow participants' money to be so freely embezzled. The amicus, The Insurance Company Benefits Group and the American Council of Life Insurance, basically argued that insurance companies need the protection afforded herein by the Second Circuit. The DOL as amicus argued that the participants need the protection sought in this litigation which has been provided to them by ERISA.

OPINIONS BELOW

The Second Circuit's opinion is reported at 138 F.3d 98 (2nd Cir. 1998), and is reprinted in the Appendix hereto at A-1a.[4] The Order denying the petition for rehearing and suggestion for rehearing en banc is reprinted at A-72a. The District Court's two unpublished Orders granting respondents' motions to dismiss are reprinted at A-21a and A-38a.

JURISDICTION

The Second Circuit entered judgment on March 10, 1998. Petitioners filed a timely petition for rehearing and suggestion for rehearing en banc; the Second Circuit denied the petition on April 27, 1998. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

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[4] References to the Appendix will hereinafter begin with "A-" followed by the appropriate page number.

PERTINENT STATUTORY PROVISIONS

The statutory provisions involved in this case are ERISA §§ 404 and 405, 29 U.S.C. §§ 1104 and 1105, and for tax exemption, 26 U.S.C. § 401(k). Applicable portions thereof have been set forth in the legal points herein.

STATEMENT OF THE CASE

A. MUTUAL BENEFIT LIFE INSURANCE COMPANY

Unitron Graphics, Inc. ("Unitron") as the employer and plan sponsor created three tax-deferred retirement plans. The first, a profit sharing plan covering all of its employees, is not involved in this litigation by virtue of all of its assets being embezzled. The second and third retirement plans, which are directly involved in this litigation, were salary deferral plans referred to as individual account plans. The trust agreements for each plan, one for union employees and one for non-union employees, were identical. Both the union and non-union individual account plans are directly involved in this appeal, for a portion of the assets of both plans were embezzled by Jacob Zucker ("Zucker") and Aaron Fertig ("Fertig"), the two senior officers of Unitron who were appointed as trustees by Unitron, the plan sponsor.

Each of the individual account plans was created by the employer Unitron, making use of a Mutual Benefit prototype trust plan and summary plan description. This litigation was commenced by the independent fiduciary following the embezzlement by the trustees Zucker and

Fertig from the union as well as the non-union individual account plans. The arrangement with respect to the individual account plans commenced in 1988 with Mutual Benefit and continued until the embezzlement. The method by which the participants' accounts were liquidated and returned to the embezzlers' control commenced in July of 1991.

As stated by the Circuit Court at A-5a:

> On July 1, 1991, Zucker wrote to Mutual Benefit to cancel the contract. The letter was on Unitron stationery and was signed by Zucker as trustee. The letter requested that Mutual Benefit return the plan funds to Unitron, along with an accounting breakdown for each plan participant. Mutual Benefit did not send the funds to Unitron, apparently because the funds could not properly be paid to the company but only to the trustees in their fiduciary capacity.

Whether this after-the-fact supposition by the Second Circuit is valid is arguable, as the record contains no supporting documentation to verify such conclusion.

The record is silent as to what transpired during the period between Mutual Benefit's implied rejection of the July 1, 1991 letter and August 15, 1991, when a second letter was sent, similarly on plan sponsor stationery signed by Zucker alone. The second letter of August 15, 1991, is characterized by the court as one that "instructed that the

assets of the plan be remitted to the Unitron Graphics, Inc. profit sharing trust." (A-5a).

The court makes no comment on the stark differences between the letter of July 1, 1991 and the letter of August 15, 1991. The court does point out that at the time the August 15th letter was received and acted upon, one type of investment account was subject to a New Jersey court order of July 16, 1991 which placed Mutual Benefit under supervision, and such account could not be transferred. The court, realizing that the plan could not be totally terminated, as requested in the first letter of direction, construes the second letter of direction which requested "the release" of four of the five investment accounts, as equivalent to a termination. This interpretation was judicially justified because the fifth investment account was subject to "the State Court Rehabilitation Order barring payment of funds." (A-5a at footnote 3). There is not a word in the record below reflecting any authority to "release . . . investments." There is not a word written in any document which allows investment accounts chosen by participants to be liquidated and a check to be drawn to the trust upon a requested "release of investments." The total disregard of the participants' rights cannot be justified by an after-the-fact assumption giving meaning to words at variance with the common understanding of those words.

The second letter of direction was followed by Mutual Benefit. Respondent Helene Gorny, who made the decision to transfer the funds and who made the decision to liquidate certain accounts and transfer the funds, exercised direct control over participants' accounts and saw to their liquidation and transfer. The participants who fortuitously

elected investments in the account blocked by the rehabilitation proceedings, have the State of New Jersey to thank for their retirement income.

As a result of the liquidation of the designated accounts, the sum of $239,811.28 was transferred to the account maintained by the trustees of Unitron, from which $130,000 was promptly embezzled by Zucker and Fertig, the two senior officers of the plan sponsor who, by their designation as trustees, were the signatories on the trust account.

This response to patently improper directions was held by the Second Circuit as exculpatory because, "[a]s fiduciaries, Mutual Benefit and Gorny were required to act in compliance with the contract and the plan terms. Thus, the District Court found that the transfer of funds pursuant to Zucker's instruction did not constitute a breach of fiduciary duty." (A-9a). The court then stated, "Mutual Benefit had no duty of inquiry pursuant to 1104(a)(1)(B) prior to releasing plan funds to Zucker. It had no reason to be suspicious of Zucker's cancellation of the contract . . .". (A-11a).

The court below clearly sets forth that Mutual Benefit followed an imperfect and flawed letter of direction from a trustee of the individual account plan to turn over to the trustees certain designated accounts. The court highlights that Mutual Benefit was, by its own agreement with the Plan sponsor and the trustees, only authorized to turn over participants' money to the Plan in the case of a termination. This requirement was graciously forgiven by the courts below. The Second Circuit, rejecting the initial contention that only a participant can liquidate his/her

account, as liquidation is an investment decision, states that the contract provides that only in the event that the Plan was terminated could the assets be turned over to the Plan trustees. Graciously forgiven was the fact that this Plan could not be terminated as there existed an impediment to its termination; namely, the orders of the New Jersey courts issued during the Mutual Benefit rehabilitation proceedings. Therefore, there existed a legal impediment to the termination of the Plan, a fact well known to Mutual Benefit. Nor did there exist an iota of authority to liquidate and release designated accounts. The court's factual holding is that any direction to the investment fiduciary, no matter how far from the reality of what is actually transpiring, no matter how far removed from the trust agreements' requirements, must be complied with.

The decisions of the courts below thoroughly document that not even the slightest inquiry was made of any participant, not even a simple request for confirmation was made to the participant (i.e., "since you alone make the investment decision, do you approve of Mutual Benefit's liquidating your account and transferring the monies therein to the trust fund's checking account?") Not even a simple request for confirmation to the embezzling trustees was made (i.e., "since you are not, pursuant to our own agreements, an investment fiduciary, and we are directed to send you $239,811.00, do you, in accordance with § 412 of ERISA (29 U.S.C. § 1112), have in place a fidelity bond?"). Not even a simple request for confirmation to the Plan sponsor was made (i.e., "we have been informed that the Plan is being terminated. Would you please forward to us copies of the notification thereof forwarded to the Internal Revenue Service pursuant to 29 C.F.R. 2617."). Any one of these three requests would

have produced a negative response and would have alerted Mutual Benefit that the instruction contained in the August 15, 1991 letter lacked legitimacy.

Not only were the courts forgiving of Mutual Benefit's dereliction of its fiduciary duty to the participants, but they ignored the basic inconsistency in Mutual Benefit's claim that it had to rely on written instructions from the trustees. The fact that the written direction relied upon was signed by only one trustee instead of two was likewise forgiven by the courts. In the agreements among the sponsor, the trustees, and Mutual Benefit, such a requirement could not be overlooked without further written implementation with respect to a single signatory. Also pardoned by the courts was that payment was made pursuant to a second letter of instruction. The first letter of instruction which directed that all of the sums, even those subsequently frozen by the Insurance Department of the State of New Jersey, be transferred, was not honored by Mutual Benefit. No matter what the reason ascribed by Mutual Benefit in not following the first letter of instruction was, it undercuts Mutual Benefit's and the court's position that blind obedience of a fiduciary to directions is a justifiable defense. The letters of July 1, 1991 and August 15, 1991 are clearly documents which call for a duty of inquiry by a fiduciary. Mutual Benefit followed that duty upon receipt of the first letter, but now argues that no such duty existed with respect to the second letter. The courts below somehow ignored this pertinent fact. Upon receipt of the funds by draft dated August 30, 1991 for $239,811.28, Zucker and Fertig immediately appropriated by embezzlement for themselves the sum of $130,000.

B. PRINCIPAL MUTUAL LIFE INSURANCE COMPANY

The Second Circuit then turns its attention to the facts impacting upon Principal, which antedated the August 30, 1991 draft. The court states:

> On July 2, 1991, prior to receiving plan funds from Mutual Benefit but after sending the first letter canceling Mutual Benefit's contract, Zucker entered into a new group annuity contract with Principal under which Principal agreed to manage the plan. Zucker and Fertig were named trustees under the contract.
>
> On September 17, 1991, Howard Lowett, Unitron's Vice-President of Administration, sent Principal a letter stating that "I am enclosing a breakdown of the check that was sent to us by Mutual Benefit Life," and detailing each plan participant's assets. The breakdown totalled $239,811.28, the amount of the check remitted by Mutual Benefit to Zucker.
>
> On October 8, 1991, Principal received a wire transfer in the amount of $109,811.28. Principal was unable to allocate the money among plan participants because the amount transferred did not correspond with the breakdown sent by Lowett. (A-6a).

Following the July agreement with Principal, Unitron made contributions on behalf of the participants to the union and non-union individual account plans through salary reductions, but was in arrears with respect to its employer matching contributions. Such a significant error in and of itself should have alerted Principal of a possible breach.

On November 5, 1991, Principal sent a letter to Unitron stating that it had received only a portion of the Plan assets, and requesting verification that Principal was the only investment manager. Other deficiencies in fiduciary conduct were set forth by Principal to Unitron, which included notification of the DOL's regulations requiring that all funds be received within 90 days.

On November 14, 1991 a second letter was sent by Principal to Unitron to the effect that no allocations could be made to the participants because of the shortage of money (the $130,000 embezzled). Needless to say, Principal received no response to either letter.

As the court below pointed out, internal memos between Principal personnel stressed the gravity of the situation. The memos stressed that the missing sums "must be accounted for" (p. 7), that there could be possible penalties under ERISA § 502(l), 29 U.S.C. § 1132(l), and that the failure to rectify the situation would "require notification to the Secretary of Labor." (p. 7). Principal, having been notified of the Chapter 11 bankruptcy proceedings filed by Unitron and having been notified that employee deferral funds had been used to meet the company's operating and payroll expenses, was requested to delay notification to the DOL, which it stated it would

refuse to do. In actuality, however, Principal not only continued to delay notification but never initiated notification to the DOL or anyone else.

Principal's internal memos stated that Principal's trustees were not living up to their fiduciary obligations. Principal's files also contained interoffice memos, one of which was dated November 13, 1991 and stated: "The client has received $130,000 transfer money from Mutual Benefit and is holding onto it instead of submitting it to us. They also have not been submitting regular contributions to us." (R-687).[5] The internal memo's clearly shows the writer's failure to heed 29 U.S.C. § 1132(b(2) and specific regulations at 29 C.F.R. 2560.502-1. Two months later on January 14, 1992, a participant called and Principal's interoffice memo states:

> I received a call from Lance Burt who is an employee at Unitron Graphics. He said that Howard Lowett gave him my name to call and find out about his account. He said that he knows that his money had transferred to us from Mutual Benefit and he was wondering what he had in his account. I told him that I didn't have enough information to allocate the money received to the individual's account, but that he can be assured that his money is earning interest daily. He argued with me that we've had

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[5] References to the record submitted to the Second Circuit below will be preceded by "R-" followed by the appropriate page number.

> the money since September and I should be able to tell him something. I took his name and number . . . and told him that I had to check with a couple of people and someone would call him back.
>
> (This is the case that the employer has been holding the monies and not submitting them. Our legal department is involved.) (R-689).

A second interoffice memo, sent just 15 minutes later, further compounded the situation by stating, "I explained to Lynn that we did not want any call from participants calling the home office for info, plus we felt it was not for us to tell them what the status is on the case." (R-688). The Second Circuit ignored the general rules of law that fiduciaries cannot lie, mislead or misinform a participant, nor can fiduciaries remain silent when a problem is discernible by them.

The heart of the defense raised by Principal is contained in the Second Circuit's opinion where it states, "Zucker and Fertig were subsequently indicted for bank fraud, embezzlement, filing of false documents with the IRS, and conspiracy to embezzle funds. Both defendants pleaded guilty to conspiracy to embezzle funds and were ordered to pay restitution. Zucker and Fertig proved to be insolvent." (A-8a) The Second Circuit concluded, "[t]he District Court found that Principal was entitled to summary judgment because of the plaintiff's failure to satisfy the additional requirement of § 1109(a) by showing that the funds loss resulted from Principal's inaction." (A-15a).

Circuit Judge Leval, with respect to the obligation of showing the ability to collect from the embezzlers, states in footnote #9 that, "[h]e dissents from this ruling believing that the evidence outlined above was sufficient to give rise to a material issue of fact to present to the jury." (A-15a) With respect to Principal, the issue to be discussed in the legal points herein is simply whether the financial ability of an embezzler to satisfy a judgment should be a necessary component of the participants' prima facie case, or is it merely a defense available to the breaching fiduciary when participants make claims under §§ 404 and 405 of ERISA, 29 U.S.C. §§ 1104 and 1105.

REASONS FOR GRANTING THE WRIT

I. The Second Circuit Erred by Ignoring the Requirements of § 404(c) of ERISA, 29 U.S.C. § 1104(c), and 26 U.S.C. § 401(k).

Irrespective of any agreement entered into by a plan sponsor, its designated trustees and an insurance company as to how they will handle participants' salary reduction contributions, pursuant to § 404(c) of ERISA, 29 U.S.C. § 1104(c), and 26 U.S.C. § 401(k), only the participant makes the investment decision. Section 404(c), 29 U.S.C. § 1104(c), clearly provides:

> (c)(1) In the case of a pension plan which provides for individual accounts and permits a participant or beneficiary to exercise control over assets in his account if a participant or beneficiary exercises control over the assets in his account (as determined under regulations of the Secretary)--

> (A) such participant or beneficiary shall not be deemed to be a fiduciary by reason of such exercise, and
>
> (B) no person who is otherwise a fiduciary shall be liable under this part for any loss, or by reason of any breach, which resuls from such participant's, or beneficiary's exercise of control.

The non-investment fiduciaries and embezzlers, Zucker and Fertig, were successful in their crime because Mutual Benefit allowed an unauthorized party to make an investment decision; i.e., liquidate certain investment accounts and transfer the amount. Liquidation of an investment is an investment decision which cannot be made without knowledge, let alone approval, of the participants. The structure of individual account plans prohibits by its very nature an investment decision by any person other than the participant.

Even if the court below was willing to transfer the contents of the first letter with respect to plan termination to the second letter requesting release of accounts, the transmittal to the Fund of employee monies was violative of 26 U.S.C. § 401(k)(10)(B)(i), as neither letter speaks of "the termination of the plan without establishment . . . of another defined contribution plan." (26 U.S.C. § 401(k)(10)(A)(i).

II. The Second Circuit Erred by Holding a Direction to a Fiduciary Must be Followed, Without any Duty of Inquiry.

The Second Circuit granted exculpation to Mutual Benefit ostensibly because Mutual Benefit was following directions of a single sponsor-appointed trustee. The court held that the unquestioned following of directions forecloses all other argument. Such holding negates ERISA fiduciary responsibility by subjecting it to arrangements made by third parties as to how participants' accounts are handled, and provides freedom from liability by unswerving adherence to the contract terms. Mutual Benefit and Unitron entered into a contract as to how they would handle the participants' monies. They did so as the proverbial two gentlemen who determine what amount a third should contribute to charity. The Second Circuit ignored the effect of ERISA on the contract. However, ERISA contracts between parties other than the participants were subject to a concise analysis by Chief Judge Posner of the Seventh Circuit in Mathews v. Sears Pension Plan, 1998 U.S. App. LEXIS 9562, pp. 5-6 (7th Cir. 1998), where the court stated:

> The parties agree that the ordinary principles of contract interpretation govern the interpretation of pension plans covered by ERISA. Cases can easily be cited for this proposition. . . But like so many legal generalizations, this one requires qualification to be completely accurate. First, when the fiduciary aspects of a plan are in issue, the relevant principles are those of the law of trusts rather than the law of

> contracts. . . Second, the relevant principles of contract interpretation are not those of any particular state's contract law, but rather are a body of federal common law tailored to the policies of ERISA. . . And third, when a case involves ERISA pension plans rather than ERISA welfare plans, the interpretive principles also are to be tailored to the distinctive characteristics of pension plans. . . . (Citations omitted.)

Even the most directed of fiduciaries has the obligation of inquiry. Even insurance contracts cannot waive participants' rights. A clause in a contract cannot act to limit any fiduciary duty, including that of investigation and inquiry. See Harris Trust and Savings Bank v. Salomon Bros., 1996 U.S. Dist. LEXIS 8485 (N.D.Ill. 1996). In addition, such provision is not binding on the plan participants. See Central Pa. Teamsters Pension Fund v. McCormick Dray, 85 F.3d 1098 (3rd Cir. 1996).

Mutual Benefit was not acting in accordance with any directions of the ultimate beneficiaries or participants. It was acting upon the alleged directions of one who, according to Mutual Benefit's trust agreement, was not an investment fiduciary. Therefore, at a minimum, Mutual Benefit was under a duty to make a reasonable inquiry and investigate whether Zucker had breached his duty. As the Eighth Circuit held:

> When the direction comes from another fiduciary, as it did in this case, the law of

trusts does not excuse a compliant trustee from all fiduciary responsibility:

> [W]here the holder of the power [to direct the trustee] holds it as a fiduciary, the trustee is not justified in complying with his directions if the trustee knows or ought to know that the holder of the power is violating his duty to the beneficiaries as fiduciary in giving the directions.

IIA Scott on Trusts § 185, at p. 574 (4th ed. 1987). We conclude from the limitation in § 1103(a) to directions "not contrary to this chapter" that Congress adopted this standard in ERISA. Thus, an ERISA trustee who deals with the plan assets in accordance with proper directions of another fiduciary is not relieved of its fiduciary duties to conform to the prudent man standard of care, see 29 U.S.C. § 1104(a) . . . .

Firstier Bank N.A. Omaha v. Zeller, 16 F.3d 907, 911 (8th Cir.), cert. denied, 513 U.S. 871 (1994).

A fiduciary's obligation to a participant is only extinguished when adequate provisions have been made for the continued prudent management of plan assets. See Chambers v. Kaleidoscope, Inc. Profit Sharing Plan and Trust, 650 F. Supp. 359, 369 (N.D. Ga. 1986); Pension Benefit Guaranty Corp. v. Greene, 570 F. Supp. 1483, 1488 (W.D. Pa. 1983), aff'd, 727 F.2d 1100 (3d Cir.), cert. denied, 469 U.S. 820 (1984); Freund v. Marshall &

Ilsley Bank, 485 F. Supp. 629, 635 (W.D. Wis. 1979). Simply by conveying trust assets to another willing to serve does not relieve Mutual Benefit of its obligations. II Austin Wakeman Scott & William Franklin Fratcher, The Law of Trusts, § 106 (4th ed. 1987).

The protection which ERISA affords would be vitiated if a fiduciary was simply able to walk away from a plan, as Mutual Benefit has done in this case. In re UNISYS Savings Plan Litigation, 74 F.3d 420, 434 (3d Cir. 1996).

Section 404 of ERISA, 29 U.S.C. § 1104, provides that the fiduciary discharges his duties "with respect to as plan solely in the interest of the participants . . . (A) for the exclusive purpose of: (i) providing benefits to participants . . .". There is not one word in the documents submitted below by defendants-appellees that their action or lack of action was calculated to be in the "interest of the participants."

Every fiduciary, in acquitting the obligation of care, skill and prudence, thus has a duty of inquiry. In this case, Mutual Benefit made no inquiry whatsoever. No inquiry was made as to why a single trustee, who by agreement was relieved of the fiduciary duty of investment, had issued a direction to transfer certain pension accounts. The second letter written by Zucker contained an investment decision, which had nothing to do with the termination of the plan, nor anything to do with termination of the contract. There is not a single document in the record, whether it be the trust agreement or the contract, to which Mutual Benefit can argue justifies such a request, or Mutual Benefit's compliance. Mutual Benefit failed to

follow the terms and conditions of the plans, and as a result, substantial damage in the amount of $130,000.00 was inflicted upon the participants. Though the courts below have disagreed, it remains clear that such a clear violation of fiduciary duties should not go unpunished.

III. Co-Fiduciary Liability Cannot be Avoided by a Claim of a Co-Fiduciary in Breach of His Obligations that the Participant must Prove that Another Breaching Fiduciary can Respond in Damages.

The proper exercise of fiduciary duty will prevent those intent on embezzlement or fraud from accomplishing their illegitimate ends. The criminal conviction of Zucker and Fertig accomplishes society's ends, but it is not a bar to Principal's liability for its flagrant breaches of fiduciary duty. By its decision below, the Second Circuit announced to all participants that ERISA has done all it can do once the embezzling fiduciaries are insolvent and in jail. In response to the complaint that Principal breached its fiduciary duties by purposefully secreting the embezzlement, failing to report the embezzlement pursuant to statute, and either lying to or at least misleading those participants who made inquiry (see Fisher v. Philadelphia Electric, 96 F.3d 1533 (3d Cir. 1996), cert. denied, 117 S.Ct. 1247 (1997); Bixler v. Central Pennsylvania Teamsters Health and Welfare Fund, 12 F.3d 1292 (3d Cir. 1993); Eddy v. Colonial Life Insurance Company of America, 919 F.2d 747 (D.C. Cir. 1990)), the Second Circuit responds to the innocent participants that it must as part of a prima facie case prove the financial ability of the embezzler to respond in damages. Thus, inaction by a

breaching co-fiduciary has no judicial value to these innocent participants.

The imposition of liability on Principal is clear pursuant to ERISA § 405, 29 U.S.C. § 1105:

> (a) In addition to any liability which he may have under any other provision of this part, a fiduciary with respect to a plan shall be liable for a breach of fiduciary responsibility of another fiduciary with respect to the same plan in the following circumstances:
>
> (1) if he participates knowingly in, or knowingly undertakes to conceal, an act or omission of such other fiduciary, knowing such act or omission is a breach;
>
> * * *
>
> (3) if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach.

The participants have clearly shown liability in accordance with § 405 of ERISA, 29 U.S.C. § 1105. Principal concealed a known breach of fiduciary duty. Principal made no effort to remedy the breach. 29 U.S.C. § 1105 contains no "but for" analysis adding a burden on the participant that he/she must prove the financial worth of another embezzling fiduciary. It is submitted that there are remedial actions which would be reasonable before

litigation is commenced. Litigation is not the only option available.

If the funds of Principal were to be so carefully preserved, the cost of writing to the DOL would not be an undue expenditure. See 29 C.F.R. 2560.502-1. If Principal's assets were to be so jealously guarded, notification to the participants, rather than secretion and misleading, would not have consumed too many of Principal's dollars. Perhaps the amount of fees received by Principal and the benefit it enjoyed by adding Unitron's Plan assets to its pool of investment monies might be the proper measure by which to determine if Principal should have investigated into the advisability of commencing litigation to see if the Plan would have benefitted.

If a paid fiduciary is in breach of his duties, it is incumbent upon that fiduciary to expend its own assets to remedy the breach or to show in defense that no matter what the expenditure, no financial recovery could have been made.

The Eighth Circuit initially joined in the "but for" analysis of recovery in litigation as the participants' burden in Herman v. Mercantile Bank, as amended, 137 F.3d 584 (8th Cir. 1998); reh'g denied, 1998 U.S. App. LEXIS 7210 (8th Cir. 1998). The Eighth Circuit, synthesizing the argument, stated at 586:

> The Secretary argues Schwent breached his fiduciary duty by not bringing a lawsuit against Lenco for the unpaid health claims. At the district court, Schwent responded that bringing a lawsuit against

> Lenco would not have been prudent for the following reasons: . . . .

The reasons for not commencing litigation were bedrocked upon the financial harm that would have been done to the plan sponsor, probably forcing the sponsor into bankruptcy at an earlier point in time. The court in resolving the issue as to a lawsuit against the plan sponsor held:

> We conclude that in order to prove a breach of fiduciary duty for failure to pursue any lawsuit, the Secretary must prove a lawsuit would be successful and advantage the beneficiaries of the plan. If a fiduciary won a judgment in a lawsuit against an employer but remained unable to collect on that judgment, the lawsuit would waste the resources of both the plan and the employer. Therefore, in this case the Secretary needed to prove that if Schwent pursued a lawsuit, the health plan would have benefitted.

Mercantile Bank at 587.

The Secretary then moved in the Eighth Circuit for clarification which was granted on April 2, 1998. The Secretary stated in her application:

> However, this Court also held that the Secretary had the burden to demonstrate that any successful suit would have benefitted the plan. The Secretary believes that this second holding is relevant to loss, not liability, and therefore unnecessary to

> this Court's ruling against the Secretary. Upon finding that Schwent was prudent in his decision not to file suit, this Court did not have to reach an issue bearing on the amount of possible loss to the plan (i.e., whether a suit would have benefitted the plan). [Citing Martin v. Feilen, 965 F.2d 660, 671 (8th Cir. 1992), and Roth v. Sawyer Cleater Lumber Co., 16 F.3d 559, 602, 605 (8th Cir. 1995)].

The Secretary of the DOL further disagreed with the concurrence of the Second Circuit:

> The Secretary therefore disagrees with the concurrence in Silverman v. Mutual Benefit Life Ins. Co., ____ F.3d ___, 1998 WL 105250 (2d Cir. 1998) (majority concurrence) (copy attached). In Silverman the concurrence held that in order to prove a breach of duty, the ERISA plaintiff also had to proffer some evidence that the party which had misappropriated plan assets had funds which the fiduciary could have attached to make good the loss. Silverman, 1998 WL 105250, *7. Recognizing that Feilen was inconsistent with this holding, the Silverman concurrence tried to distinguish itself by arguing that the issue in Silverman was one of causation while the issue in Feilen was one of damages. Silverman, 1998 WL 105250, *9 n 1 [footnote omitted].

> In other words, the Silverman majority concurrence read the Feilen and Roth decisions as addressing damages and not liability, which is contrary to what this Court held in this case. The Secretary agrees with the Second Circuit's reading of Eighth Circuit precedent and believes that the Silverman majority concurrence would not have erred had it adopted this Circuit's reasoning as controlling. Instead, however, the Silverman majority concurrence rejected this Circuit's reasoning and, in the Secretary's view, incorrectly applied the common law of trust's rule in fashioning relief under ERISA. See Feilen, 965 F.2d at 671; Roth II, 61 F.3d at 604. See also, Varity Corp. v. Howe, 116 S.Ct. 1065, 1070-1079 (1996) (common law of trusts guides interpretation of ERISA's provision in light of "special nature and purpose of employee benefit plans"); Donovan v. Bierwirth, 754 F.2d at 1056 [footnote omitted]. Since the common law of trusts places on the breaching fiduciary the burden to disprove loss, the Silverman majority concurrence is incorrect.

The Eighth Circuit, in granting the clarification sought by the Secretary of Labor in Herman v. Mercantile Bank, held, "Moreover, in light of the record, Schwent might have presented a valid defense by meeting his burden of proving that no benefit would accrue to the plan by a successful lawsuit against Lenco because of Lenco's greatly

impaired financial condition." 1998 U.S. App. LEXIS 7496, p. 1.

The Second Circuit approach to the participants' burden is also at variance with Kemmerer v. ICI Americas, Inc., 70 F.3d 281, 190 (3d Cir. 1995), cert. denied. 517 U.S. 1209 (1996) (noting that in certain ERISA cases courts have placed the burden of proof on the trustee of the plan where a breach and a definitive loss were proven, but noting that neither of the prerequisites to burden shifting were present in that case). Shifting the burden of showing that the loss was not a result of the breach to the breaching fiduciary "is an appropriate federal rule of fiduciary obligation. . ." Nedd v. United Mine Workers of America, 556 F.2d 190, 211 (3d Cir. 1977), cert. denied, 434 U.S. 1013 (1978). Other circuit courts that have addressed this issue have reached conflicting results. Compare Roth, 16 F.3d at 920 (once the plaintiff shows a breach of duty and a prima facie case of loss to the plan, the trustee then has the burden of persuasion to show that the loss was not caused by the breach); and McDonald v. Provident Indem. Life Ins. Co., 60 F.3d 234, 237 (5th Cir. 1995), cert. denied, 516 U.S. 1174 (1996).

Principal deliberately chose to do nothing. As set forth, filing a claim in Unitron's bankruptcy proceeding, notifying the DOL and/or, more importantly, notifying the participants, are not expensive endeavors. As Judge Friendly commented, "Courts do not take kindly to arguments by fiduciaries who have breached their obligations that, if they had not done this, everything would have been the same." In re Beck Indus., Inc., 605 F.2d 624, 636 (2d Cir. 1979). See also Bogert, The Law of Trusts & Trustees § 971 (2d revised ed. 1995) ("If the

beneficiary shows a prima facie case, the burden of contradicting it or showing a defense will shift to the trustee"); Restatement (Second) of Trusts § 212(4) (1959).

Having deliberately chosen no action but instead engaged in subversion of the truth, Principal bears liability under ERISA, for its clear violation of § 405(a)(1)(3), 29 U.S.C. § 1105(a)(1)(3), for Principal "in addition to any liability which [it] may have under any other provisions of this part . . . shall be liable for the breach of fiduciary responsibility of another fiduciary with respect to the same plan."

CONCLUSION

For the foregoing reasons, this Court should grant the petition for a writ of certiorari, and either summarily reverse the judgment below or set the case for plenary review.

Respectfully submitted,

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Petitioner Independent Fiduciary

APPENDIX

APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT DECIDED MARCH 10, 1998

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 768—August Term, 1996

(Argued: June 2, 1997 Decided: March 10, 1998)

Docket No. 96-7795

DAVID W. SILVERMAN, as Independent Fiduciary of The Unitron Graphics, Inc. Profit Sharing Trust and Unitron Graphics, Inc. Profit Sharing Trust-Union and Non-Union Division,

Plaintiff-Appellant,

—v.—

MUTUAL BENEFIT LIFE INSURANCE COMPANY, PRINCIPAL MUTUAL LIFE INSURANCE COMPANY and HELENE GORNY,

Defendants-Appellees,

JACOB ZUCKER and AARON FERTIG,

Defendants.

Before:

MESKILL, JACOBS, and LEVAL,

Circuit Judges.

Appendix A

Appeal from orders of the United States District Court for the Eastern District of New York (Ross, *J.*) granting summary judgment in favor of defendants Principal Mutual Life Insurance Company, Mutual Benefit Life Insurance Company, and Helene Gorny.

Affirmed. Judge Jacobs's concurrence is set forth in part in a separate opinion. Judge Leval dissents in part.

DAVID W. SILVERMAN, New City, N.Y., (Christopher P. Tirro, Granik Silverman, et al., New City, N.Y., Of Counsel), *for Plaintiff-Appellant.*

GEORGE BERGER, New York, N.Y., (Bruce J. Turkle, Phillips Nizer Benjamin Krim & Ballon, LLP, New York, N.Y., Of Counsel), *for Defendants-Appellees, Mutual Benefit Life Insurance Company and Helene Gorny.*

HOWARD S. WOLFSON, New York, N.Y., (Patricia Anne Kuhn, Whitman Breed Abbott & Morgan, New York, N.Y., Of Counsel), *for Defendant-Appellee, Principal Mutual Life Insurance Company.*

GARY S. TELL, Washington, D.C., (J. Davitt McAteer, Marc. I. Machiz and Karen L. Handorf, Attorneys for the Secretary of Labor, Washington, D.C.), *Amicus Curiae, Department of Labor.*

Thomas S. Gigot, Kathryn A. English, Groom and Nordberg, Chtd., Washington, D.C., *Amicus Curiae, The Insurance Company Benefits Group.*

Appendix A

Beth Heifetz (Counsel of Record), Patricia Dunn, Jones, Day, Reavis & Pogue, Washington, D.C., Philip E. Stano, American Council of Life Insurance, Washington, D.C., *Amicus Curiae, The American Council of Life Insurance.*

LEVAL, *Circuit Judge*:

David Silverman ("Silverman"), independent fiduciary of the Unitron Graphics, Inc. Profit Sharing Trust and the Unitron Graphics, Inc. Profit Sharing Trust—Union and Non-Union Division (the "plan"),[1] brought this suit against Mutual Benefit Life Insurance Company ("Mutual Benefit"), a Mutual Benefit employee named Helene Gorny ("Gorny"), and Principal Mutual Life Insurance Company ("Principal"), pursuant to the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. §§ 1001 *et seq.* Mutual Benefit administered the plan and invested its funds under contract with the plan. Principal took over plan administration and investment after Mutual Benefit's contract was terminated. After Mutual Benefit's administration was terminated, but before Principal received the plan funds, Jacob Zucker and Aaron Fertig, the two plan trustees, embezzled $130,000 in plan funds. Silverman sued Mutual Benefit, Gorny, and Principal on the theory that their violation of various ERISA provisions allowed the embezzlement to occur and prevented recovery of plan funds after the embezzlement.[2] The United States District

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[1] Unitron established separate plans for union and non-union employees. Since the two plans are identical in all relevant respects, they will be referred to as a single plan.

[2] Silverman does not seek any relief against Zucker and Fertig in this proceeding.

Court for the Eastern District of New York (Ross, *J.*) granted summary judgment in favor of defendants on all counts.

Silverman alleges that Mutual Benefit and Gorny are personally liable for loss to the plan because, when Mutual Benefit's contract was terminated, they returned the plan's funds to Zucker upon his written request. Mutual Benefit's actions were required under the terms of the plan and Mutual Benefit's contract with the plan. Mutual Benefit's return of plan funds was consistent with the summary plan description (the "SPD") and complied with all relevant Department of Labor ("DOL") regulations. The return of the funds cannot constitute the basis for a finding that Mutual Benefit or Gorny breached their ERISA fiduciary duties, and summary judgment in their favor was properly granted.

Silverman contends Principal should be liable under 29 U.S.C. § 1109(a) because it failed to take steps to remedy the fiduciary breach committed by Zucker and Fertig in violation of 29 U.S.C. § 1105(a)(3). The district court granted summary judgment to Principal because Silverman had failed to produce evidence from which a jury could find that, at the time of Principal's alleged breach, Zucker or Fertig had money that might have remedied the loss. The majority of our panel agrees. The grant of summary judgment in favor of Principal is therefore affirmed as well.

Background

The parties do not dispute the facts giving rise to this action. In 1988, Unitron Graphics, Inc. ("Unitron") established the plan for employee profit-sharing. It was established as an "individual account" or "defined contribution" ERISA plan under 29 U.S.C. § 1002(34). Each participating employee could elect to have Unitron set aside part of his

salary as a contribution to the plan; in addition, the company could make matching and discretionary contributions.

The plan had two named trustees: Jacob Zucker and Aaron Fertig, who were owners and officers of Unitron. The plan provided that joint trustees "shall act by a majority of their number but may authorize one or more of them to sign all papers on their behalf." It further provided that Mutual Benefit "may rely on the signature of any Trustee on . . . any document used in connection with" a plan-related contract.

The plan's assets were invested pursuant to a group annuity contract between the trustees and Mutual Benefit. The trustees retained the right to cancel the contract at any time.

Mutual Benefit experienced well-publicized financial problems in the Spring and Summer of 1991, which culminated in a July 16, 1991, order of the Superior Court of New Jersey placing Mutual Benefit into court-supervised rehabilitation.

On July 1, 1991, Zucker wrote to Mutual Benefit to cancel the contract. The letter was on Unitron stationery and was signed by Zucker as trustee. The letter requested that Mutual Benefit return the plan funds to Unitron, along with an accounting breakdown for each plan participant. Mutual Benefit did not send the funds to Unitron, apparently because the funds could not properly be paid to the company but only to the trustees in their fiduciary capacity.

On August 15, 1991, Zucker, as plan trustee, wrote a second letter to Mutual Benefit. This letter instructed that the assets of the plan[3] be remitted to the Unitron Graphics Inc. Profit Sharing Trust with a breakdown by participant.

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[3] The instructions related to only four of the plan's five investment accounts. The fifth investment account was subject to the state court rehabilitation order barring payout of funds.

Accordingly, Mutual Benefit liquidated the fund's investments and defendant Gorny, a Mutual Benefit customer service supervisor, approved a check requisition. On August 30, 1991, Mutual Benefit sent Zucker a check for the proceeds in the amount of $239,811.28 payable to the plan.

Zucker deposited the check in the plan's bank account on September 6, 1991. Over the next few weeks, Zucker and Fertig embezzled $130,000 from the account.

On July 2, 1991, prior to receiving plan funds from Mutual Benefit but after sending the first letter cancelling Mutual Benefit's contract, Zucker entered into a new group annuity contract with Principal under which Principal agreed to manage the plan. Zucker and Fertig were named trustees under the contract.

On September 17, 1991, Howard Lowett, Unitron's Vice President of Administration, sent Principal a letter stating that "I am enclosing a breakdown of the check that was sent to us by Mutual Benefit Life," and detailing each plan participant's assets. The breakdown totalled $239,811.28, the amount of the check remitted by Mutual Benefit to Zucker.

On October 8, 1991, Principal received a wire transfer in the amount of $109,811.28. Principal was unable to allocate the money among plan participants because the amount transferred did not correspond with the breakdown sent by Lowett.

On November 5, 1991, Principal sent a letter to Unitron, addressed to Zucker and Fertig as trustees of the plan. Principal stated that it had "received, from what limited record-keeping data we have, only a portion" of the plan assets liquidated by Mutual Benefit. Principal noted that "[i]t is our understanding that we are to be the only investment manager for your profit sharing plans," and requested that Zucker and Fertig forward the balance of the funds. Principal also noted that employee salary deferral contributions had not been for-

warded in the four months since the plan entered into its contract with Principal, although DOL regulations required that they be forwarded within ninety days of their receipt. Principal received no answer.

On November 14, 1991, Principal sent a second letter to Lowett, explaining that "[u]ntil this deposit's allocation is complete, we will place your deposit into an unallocated account." Once again, Principal did not receive a response.

Internal memos indicate that by mid-November Principal recognized the possible existence of a legal problem arising from the missing $130,000 and the apparent failure to submit employee deferral contributions. On January 28, 1992, Principal sent another letter to Zucker and Fertig, in which it noted that the missing $130,000 "must be accounted for," and threatened to refuse to accept additional funds if Zucker and Fertig did not produce the $130,000 or explain its absence within five business days. The letter also noted the failure to remit outstanding employee deferral amounts as required by federal regulation, and asserted that ERISA § 502(l) would require notification to the Secretary of Labor if the funds were not turned over within five business days.

Several days later, Principal received a phone call from a Arnold Freilich ("Freilich"), a consultant acting as representative for Unitron. Freilich advised that Unitron had filed for Chapter 11 bankruptcy and requested that Principal delay informing the DOL about the delinquency in forwarding employee deferral amounts until a buyer could be found for the business. Freilich informed Principal that Zucker had used the employee deferral funds to meet the company's operating and payroll expenses. Principal told Freilich that it would not delay notifying the DOL about delinquencies; however, no such notification was made. On February 13, an internal memorandum at Principal stated that "the group rep . . . became aware that the trustees were not living up

to their fiduciary responsibilities. . . . Legal has been involved."

On March 30, 1992, the DOL wrote Principal to inquire about the status of the plan, the rollover of funds from Mutual Benefit, and employee deferral contributions. On April 2, 1992, Principal sent copies of relevant documents and letters to the DOL disclosing the missing $130,000 and the delinquencies in salary deferral contributions. The DOL was unable to recover any funds in the course of its investigation.

Zucker and Fertig were subsequently indicted for bank fraud, embezzlement, filing of false documents with the IRS, and conspiracy to embezzle funds. Both defendants pleaded guilty to conspiracy to embezzle funds and were ordered to pay restitution. Zucker and Fertig proved to be insolvent. Although a portion of the embezzled funds has been replaced, it appears that the money came primarily from loans and gifts from third parties.

Plaintiff Silverman was appointed as independent fiduciary of the plan with authority to seek recovery of the remainder of the plan assets. Silverman commenced this action against Mutual Benefit, Helene Gorny, and Principal. In his amended complaint, Silverman alleges that defendants violated 29 U.S.C. §§ 1104 and 1105. Silverman claims that the transfer of funds from Mutual Benefit pursuant to Zucker's instructions violated 29 U.S.C. § 1104(a)(1)(D) because it was "not in accordance with any term or provision of the summary plan description," not in accordance with the annuity contract between Mutual Benefit and the plan, and not in accordance with the terms of the plan itself. The complaint also charges that Mutual Benefit violated 29 U.S.C. § 1104(c) by transferring the plan funds to the trustees. Gorny is alleged to have acted without the requisite care, skill, prudence, and

diligence in approving the transfer, in violation of 29 U.S.C. § 1104(a)(1)(B). As to Principal, the complaint alleged that it violated 29 U.S.C. § 1105(a)(2) and (3) by failing to investigate and take action to recover the missing plan funds.[4]

The district court granted summary judgment in favor of defendants Mutual Benefit and Gorny. Under the terms of its contract with the plan and the plan itself, Mutual Benefit was required to turn over all plan funds upon written demand by a trustee. As fiduciaries, Mutual Benefit and Gorny were required to act in compliance with the contract and the plan terms. Thus, the district court found that transfer of funds pursuant to Zucker's instructions did not constitute a breach of fiduciary duty.[5]

The district court also granted summary judgment in favor of defendant Principal. The court explained that the sole jurisdictional basis for a suit seeking money damages was 29 U.S.C. § 1132(a)(2), which allows suits for violations of 29 U.S.C. § 1109(a). Under § 1109(a), Principal would be liable for any breach of its fiduciary duty under 29 U.S.C. § 1105(a) only for losses to the plan "resulting from" such breach. 29 U.S.C. § 1109(a). The court concluded that Silverman had failed to offer any evidence that the plan's loss resulted from Principal's breach.

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[4] Although Silverman's complaint refers solely to 29 U.S.C. §§ 1105(a)(2)-(3), he argued to the district court that Principal's actions also violated 29 U.S.C. § 1105(a)(1).

[5] The district court also rejected Silverman's contention that the SPD inadequately described or misrepresented the possibility of transfer of plan funds from Mutual Benefit to Zucker.

Appendix A

Discussion

A. Mutual Benefit and Gorny

Mutual Benefit's transfer of plan funds to Zucker, in the form of a check made out to the plan, complied fully with the terms of Mutual Benefit's contract with the plan. The contract provided that Zucker, as trustee of the plan, "may discontinue this contract at any time by notifying us in writing." No other conditions are placed upon cancellation. Zucker sent Mutual Benefit a letter signed in his capacity as plan trustee "discontinuing the 401(k) Contract." Upon written notice of discontinuance, Mutual Benefit was required to return to the plan all "Investment Accounts held under this contract."

The transfer of plan funds also complied fully with the terms of the plan itself. Silverman argues that Mutual Benefit and Gorny violated their fiduciary duties of care and prudence by transferring the plan funds because Zucker's letter requesting cancellation of the contract was signed by only one of the two plan trustees. Under ERISA, a trust agreement providing for more than one fiduciary must provide for joint authority to control and manage the plan, *see* 29 U.S.C. § 1102(a), and the exercise of joint powers typically requires the action of all trustees. *See Illinois Conf. of Teamsters and Employers Welfare Fund v. Mrowicki*, 44 F.3d 451, 462-63 (7th Cir. 1994). However, joint trustees may modify the default rule by agreeing to delegate authority to a single agent. *See id.* at 463; *see also* Restatement (Second) of Trusts § 194 (1959) (joint trustees must act unanimously "unless it is otherwise provided by the terms of the trust"). Under the terms of the plan, the joint trustees "may authorize one or more of them to sign all papers on their behalf." The plan further provided that Mutual Benefit "may rely on the signature of any Trustee on an application for or any document used in connection with" its contract with the plan. The plan

delegated to Zucker the authority to act on behalf of both trustees in documents used in connection with the plan, and Mutual Benefit lawfully relied on this authority in connection with cancellation of the contract.

Nor did the disbursement of plan funds conflict with the terms of the SPD. The SPD explained that the plan trustees retained "the right to amend or discontinue the Plan." It did not elaborate on the procedures to be followed by the trustees in taking such action, and was not required to do so. *See* 29 U.S.C. § 1022(b). Nothing in the SPD prohibited a trustee's cancellation of Mutual Benefit's contract with the plan.

Under these circumstances, Mutual Benefit had no duty of inquiry pursuant to § 1104(a)(1)(B) prior to releasing plan funds to Zucker. It had no reason to be suspicious of Zucker's cancellation of the contract. *Cf. FirsTier Bank N.A. v. Zeller*, 16 F.3d 907, 911 (8th Cir.) (bank could be liable for complying with trustee's order "if the [bank] knows or ought to know that the [trustee] is violating his duty to the beneficiaries as fiduciary in giving the directions") (quoting IIA Scott on Trusts § 185, at 574 (4th ed. 1987)), *cert. denied*, 513 U.S. 871, 115 S. Ct. 194 (1994). Mutual Benefit's financial problems in the Spring and Summer of 1991 provided ample reason for the cancellation. Zucker's cancellation request complied fully with the terms of all relevant plan documents and the contract itself. *Cf. Brandt v. Grounds*, 687 F.2d 895, 898 (7th Cir. 1982) (refusing to impose a fiduciary duty to inquire about the prudence of trustee's withdrawal of plan funds where bank had contractual duty to honor trustee's withdrawal slips). Summary judgment was properly granted in favor of Mutual Benefit and Gorny.[6]

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[6] In view of this disposition, we need not consider Mutual Benefit's contention that it was not acting as a fiduciary in transferring the plan funds to the trustees because it lacked discretionary authority in connection with that action. *See Geller v. County Line Auto Sales, Inc.*, 86 F.3d 18, 21 (2d Cir. 1996).

We do not discuss the contentions that Silverman raises for the first time on appeal, as these arguments are waived for failure to raise them below. *See Jacobson v. Fireman's Fund Ins. Co.*, 111 F.3d 261, 266 (2d Cir. 1997).

B. Principal

Silverman claims that Principal's failure to investigate and take steps to recover the $130,000 in missing plan assets constituted a breach of its co-fiduciary duties under 29 U.S.C. § 1105(a).

Under 29 U.S.C. § 1105(a), a plan fiduciary[7]

> shall be liable for a breach of fiduciary responsibility of another fiduciary . . .
>
> > (3) if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach.

Silverman argues that liability should be imposed on Principal based on Principal's failure to investigate Zucker and Fertig's embezzlement and to take reasonable steps to recover missing plan funds. *See Lee v. Burkhart*, 991 F.2d 1004, 1010-11 (2d Cir. 1993).

Like the district court, we read the relevant statutes to require Silverman to show that the loss claimed resulted from Principal's breach. Jurisdiction for this suit for compensatory damages arises under § 1132(a)(2), which permits a fiduciary to bring a civil action "for appropriate relief under section 1109 of this title."[8] Section 1109, in turn, provides

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[7] Principal meets the definition of a "fiduciary with respect to a plan" under 29 U.S.C. § 1002(21)(A)(i), (iii) (stating that a person who "exercises any authority or control respecting management or disposition of its assets" or who "has any discretionary authority or discretionary responsibility in the administration of such plan" is "a fiduciary with respect to a plan").

[8] Silverman does not contend that he has authority to sue Principal for recovery of compensatory money damages under § 1132(a)(3), although that pro-

> Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan *resulting from* each such breach . . . .

29 U.S.C. § 1109(a) (emphasis added). This statute therefore requires a plaintiff to demonstrate in a suit for compensatory damages that the plan's losses "result[ed] from" Principal's breach of § 1105(a)(3). *See Willett v. Blue Cross and Blue Shield*, 953 F.2d 1335, 1343 (11th Cir. 1992) (defendant who breaches § 1105(a) is liable under § 1109(a) for the resulting loss); *see also Free v. Briody*, 732 F.2d 1331, 1336 (7th Cir. 1984); *Justice v. Bankers Trust Co. Inc.*, 607 F. Supp. 527, 535-36 (N.D. Ala. 1985). Specifically, Silverman must show some causal link between the alleged breach of Principal's duties and the loss plaintiff seeks to recover. *See Felber v. Estate of Regan*, 117 F.3d 1084, 1087 (8th Cir. 1997); *In re Unisys Sav. Plan Litig.*, 74 F.3d 420, 445 (3d Cir.), *cert. denied*, ___ U.S. ___, 117 S. Ct. 56 (1996); *Friend v. Sanwa Bank California*, 35 F.3d 466, 469 (9th Cir. 1994); *Ironworkers Local #272 v. Bowen*, 695 F.2d 531, 536 (11th Cir. 1983); *Brandt*, 687 F.2d at 898; *see also Diduck v. Kaszycki & Sons Contractors, Inc.*, 974 F.2d 270, 279 (2d Cir. 1992) (defendant fiduciary may not be held liable for breaching fiduciary duty to pay contributions to ERISA fund "unless, absent a fraudulent breach, the funds could have collected them"). This principle is consistent with the common law of trusts, which imposes a duty on a successor trustee to remedy the breach of a prior trustee, and imposes liability for breach

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vision might authorize the recovery of equitable monetary relief for a violation of § 1105(a)(3). *See Varity Corp. v. Howe*, 516 U.S. 489, ___, 116 S. Ct. 1065, 1077-78 (1996). Compensatory damages are not "equitable relief" under the meaning of § 1132(a)(3). *See Mertens v. Hewitt Assocs.*, 508 U.S. 248, 255-59, 113 S. Ct. 2063, 2068-70 (1993).

of this duty "to the extent to which a loss results from [the successor trustee's] failure to take such [remedial] steps." *See* Restatement (Second) of Trusts § 223(2) and cmts. c. and d. (1959).

Thus, in order to satisfy the necessary elements imposed by §§ 1105(a)(3) and 1109(a), Silverman must show that (i) Principal had knowledge of the trustees' embezzlement, (ii) Principal failed to make reasonable efforts to remedy the trustees' breach, and (iii) the fund's loss resulted from that failure.

A material question of fact exists as to whether Principal had knowledge of a breach of fiduciary duty by the trustees. Principal knew that Zucker and Fertig had not forwarded all the plan assets remitted by Mutual Benefit; it knew also that Unitron had failed to make the required salary deferral contributions. Principal sent letters on November 5 and November 14 raising the issue of the trustees' failure to forward all of the plan funds. It received no answer to either letter. Principal's internal memoranda show that by November 13 it recognized that it had a legal problem and had involved its legal department. Although Principal did not know all the facts concerning embezzlement, a reasonable factfinder could conclude that, at some point prior to its report to the Department of Labor, Principal had knowledge of the trustees' breach. *See Lee v. Burkhart*, 991 F.2d 1004, 1011 (2d Cir. 1993).

Silverman has also adduced sufficient evidence to present a jury question whether Principal breached its duty under § 1105(a)(3) to "make[ ] reasonable efforts under the circumstances to remedy the breach." In the face of indications of impropriety concerning the fund's monies, Principal did nothing. Indeed, its inaction continued even after it had been told in late January or early February 1992 of the embezzlement of salary deferral contributions. The deficiency of

funds, coupled with the trustees' failure to respond to Principal's inquiries, could reasonably sustain a finding that Principal had a duty to take further action to explore the reason for the deficiency and take steps to recover the missing funds.

The district court found that Principal was entitled to summary judgment because of the plaintiff's failure to satisfy the additional requirement of § 1109(a) by showing that the fund's loss resulted from Principal's inaction. Judge Ross reasoned that Silverman had failed to make any showing that, at the time Principal's duty of pursuit arose, Zucker or Fertig had any assets that might have been recovered. As further explained in Judge Jacobs's separate opinion, a majority of our panel agrees, by reason of the absence of evidence that Zucker or Fertig had funds in November or thereafter.[9] Accordingly we affirm the grant of summary judgment in favor of Principal.

We have considered Silverman's other claims of error and find them to be without merit.

Conclusion

The judgment of the district court is affirmed.

JACOBS, *Circuit Judge*, with whom Judge Meskill concurs, concurring:

The opinion of the Court reflects the conclusion that Silverman failed to make the requisite showing under § 1109(a)

[9] The author of the opinion respectfully dissents from this ruling, believing that the evidence outlined above was sufficient to give rise to a material issue of fact to present to a jury.

that the fund's losses *resulted* from Principal's inaction. Judge Leval (as author) records his disagreement with that view and the opinion of the Court does not address it. Having signed the opinion of the Court, I write additionally to explain why Silverman has failed to adduce evidence sufficient to raise a genuine issue of material fact with respect to causation.

An ERISA plaintiff who seeks compensatory damages under § 1105(a)(3) must show, *inter alia*, that the losses "result[ed] from" the defendant's failure to take reasonable steps to remedy the co-fiduciary's breach. *See* 29 U.S.C. §§ 1109(a), 1105(a)(3) (1985); *Diduck v. Kaszycki & Sons Contractors*, 974 F.2d 270, 279 (2d Cir. 1992). Causation of damages is therefore an element of the claim, and the plaintiff bears the burden of proving it. The specific factual question is whether Zucker or Fertig, during the time period in which Principal is alleged to have violated its duty to act, possessed assets from which any portion of the embezzled funds could be recovered. The date of Principal's alleged breach of its duty to act (if any) is a question for the fact-finder; but if there was a breach, it took place on some date between mid-November 1991 and March 1992. Unless Zucker and Fertig had resources that could be found and seized to replenish the plan *at such time as Principal breached a duty to act*, the loss cannot have been caused by Principal's inaction.

Silverman has expressly declined to proffer evidence as to what Fertig and Zucker did with the funds they embezzled, or as to whether at any pertinent time they had assets that could have made good the loss. Silverman and the Department of Labor (appearing as *amicus curiae*) evidently recognize that there is no record evidence to demonstrate a causative link between Principal's inaction and the plan's losses. That is why they have argued (both in district court and on appeal)

for a shift of the burden of proof on the issue of causation, so that once a plaintiff has shown a breach of section 1105(a)(3) and a related loss, the defendant must "prove that the loss was *not* caused by its breach of fiduciary duty." Brief of the Secretary of Labor as *Amicus Curiae* at 7 (emphasis added).

This argument is derived from the common law of trusts, under which a defaulting fiduciary bears the burden of disproving causation. *See In re Beck Industries, Inc.*, 605 F.2d 624, 636-37 (2d Cir. 1979).[1] But the Supreme Court has cautioned that "the law of trusts often will inform, but will not necessarily determine the outcome of, an effort to interpret ERISA's fiduciary duties." *Varity Corp. v. Howe*, 116 S.Ct. 1065, 1070 (1996). Congress has placed the burden of proving causation on the *plaintiff* by requiring him to prove that the losses "result[ed] from" the defendant's inaction. *See* 29 U.S.C. §§ 1109(a), 1105(a)(3). And we have held that it is the plaintiff's burden to "prov[e] an amount of damages caused by the fraud." *Diduck*, 974 F.2d at 279. Section 1105(a)(3) provides for extraordinarily broad liability for co-fiduciaries because it requires only that the defendant be a fiduciary of the same *plan* as the breaching fiduciary, not that they be fiduciaries with respect to the same *assets*. So a co-fiduciary, like Principal in this case, may be held liable for another trustee's breach with respect to assets over which the defen-

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[1] The Department of Labor also relies on *Martin v. Feilen*, 965 F.2d 660, 671 (8th Cir. 1992), *cert. denied*, 506 U.S. 1054 (1993), which holds that "once the ERISA plaintiff has proved a breach of fiduciary duty and a prima facie case of loss to the plan or ill-gotten profit to the fiduciary, the burden of persuasion shifts to the fiduciary to prove that the loss was not caused by, or his profit was not attributable to, the breach of duty." Even if the Eighth Circuit's analysis is correct, the issue in *Martin* involved the *calculation of damages* after the plaintiff proved a prima facie case that the plan suffered a loss resulting from the defendant's breach of its fiduciary duty. *See id.* (holding that Secretary of Labor had established a prima facie case by proving that defendants "violated § 1104 by causing the ESOP to engage in stock transactions that caused specific injury to the ESOP *at the time in question*."). he issue before this Court involves the burden of proving causation, not damages.

dant co-fiduciary never exercised dominion or control. *See* 29 U.S.C. § 1105(a)(3).[2] The causation requirement of § 1109(a) acts as a check on this broadly sweeping liability, to ensure that solvent companies remain willing to undertake fiduciary responsibilities with respect to ERISA plans.

Silverman did not raise a fact issue as to whether Zucker and Fertig had assets at the time of the breach by showing that Zucker and Fertig had received $130,000 in late September or early October. Initially at least, an embezzler will almost always have the stolen funds in his hands. But the embezzler's initial possession of the stolen funds cannot support an inference that an embezzler maintains the funds continuously thereafter in a place accessible to creditors (subject to the defendant's showing that the funds were dissipated or hidden). Otherwise, a plaintiff who demonstrates a breach of the embezzler's fiduciary duty—a threshold requirement under section 1105(a)(3)—would often be relieved of the burden of proving causation in any meaningful sense: evidence that the embezzler once possessed the money would constitute a prima facie showing that the money could have been recovered when the co-fiduciary later failed to alert the authorities.

Why cannot a jury infer that funds in hand in September were still available in November, or the following year? The problem is that (i) the stolen funds were in the embezzlers' hands in September; but (ii) the money was gone by the following April; and (iii) the record does not show what happened to the money in the interval. A fact-finder could fix Principal's culpable failure to act on any date after mid-

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[2] Section 1105(a)(3) provides that "a fiduciary with respect to a plan shall be liable for a breach of fiduciary responsibility of another fiduciary with respect to the same plan if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach." 29 U.S.C. § 1105(a)(3) (1985).

November 1991; but Silverman has come forward with no evidence bearing on when the money vanished. So in order to decide whether—and how much—money was available for recovery at an intervening point in time, the factfinder would have no tool but speculation.

Diduck illustrates the kind of evidentiary showing required. The judgment-proof employer in *Diduck* had made no pension contributions for people working off the books, and the co-fiduciary was the shop steward whose reports to the fund trustees had failed to reflect the off-the-books employment. *Diduck*, 974 F.2d at 274. Notwithstanding the employer's chronic shortage of funds, the defendant trustees had repeatedly and successfully enforced their demands for fund contributions on behalf of reported workers by threatening work stoppages. *Id.* at 279. In light of the trustees' ability to force payments in respect of on-the-books workers, we concluded that the trial court's ruling that damages were sustained was "at most" a finding of

> what might be called a *prima facie* case of damages caused by the fraud. At that point, the defendants should have been afforded an opportunity to rebut this showing. This chance was not afforded them. After such rebuttal, the trier would have to decide whether the plaintiff had sustained his burden of proving an amount of damages caused by the fraud.

Id. Thus in *Diduck*, causation was established because the plaintiff showed that—at the time of the co-fiduciary's breach—a tool was at hand to force timely payment of amounts due; and even then, a question remained open as to whether the plaintiff had proved or could prove an *amount* of damages recoverable. Here, Silverman has declined to offer any evidence to support the fact or amount of damages, other than the underlying theft.

Silverman would have us adopt implicitly an unsupported presumption that embezzled funds are retained in an accessible place for some predictable and substantial period of time. However, "[i]t is generally understood that in law for a specified fact to be presumptive evidence of another it must be one which in common experience leads naturally and logically to that other." *Wilkins v. American Export Isbrandtsen Lines, Inc.*, 446 F.2d 480, 484 (2d Cir. 1971), *cert. denied*, 404 U.S. 1018 (1972). There is no body of common experience to establish that embezzlers as a class are so thrifty and provident that one may presume their prudent stewardship of the money they steal. The fact that Zucker and Fertig stole money in September does not support an inference that they had funds available for recovery one, two, three or four months later.

APPENDIX B — OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF NEW YORK DATED APRIL 19, 1996

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

95-CV-0500 (ARR)

David W. SILVERMAN

Plaintiff,

-against-

MUTUAL BENEFIT LIFE INSURANCE CO. et al.

Defendants.

OPINION AND ORDER

ROSS, United States District Judge:

This case arises in the aftermath of criminal wrongdoing by defendants Jacob Zucker and Aaron Fertig. Plaintiff, a court-appointed independent fiduciary of an employee benefit fund, seeks to recover money that Zucker and Fertig embezzled from the fund from two insurance companies and one individual whom he alleges were also fiduciaries of the fund under the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. §§ 1001 - 1461. Defendants Mutual Benefit Life Insurance Co. ("Mutual Benefit") and Helene Gorny have moved for summary judgment, pursuant to Fed.R.Civ.P. 56, and plaintiff has cross-moved for summary judgment against them. For the reasons

stated herein, plaintiff's motion is denied and Mutual Benefit and Gorny's motion is granted.

FACTUAL BACKGROUND

The basic factual issues in this action are essentially undisputed. On July 15, 1988, Unitron Graphics, Inc. ("Unitron") established two profit-sharing plans (collectively, the "Plan") for the benefit of its employees.[1] The Plan was qualified under ERISA and § 401(k) of the Internal Revenue Code. Zucker and Fertig, both officers of Unitron, were named as trustees of the Plan. The written agreement between Unitron and Zucker and Fertig that established the Plan was prepared by Mutual Benefit. Mutual Benefit was not a party to the agreement or a named fiduciary of the Plan, however.

The Plan was an example of what is known under ERISA as an "individual account plan" or a "defined contribution plan." *See* 29 U.S.C. § 1002(34). Each participating employee could elect to have Unitron set aside part of his salary and contribute it to the Plan. In addition, the company could choose to make matching contributions and discretionary contributions. The Plan's assets were invested in a group annuity contract (the "Contract") that Zucker and Fertig, in their capacity as trustees of the Plan,

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1. The two plans were identical, except that one was established for the benefit of union employees and one for the benefit of non-union employees. Plaintiff has sued as a fiduciary of the "Unitron Graphics, Inc., Profit Sharing Trust — Union and Non-Union Divisions," essentially treating both trusts as a single entity. Accordingly, the court treats the two plans, for purposes of this opinion, as a single entity.

Plaintiff has also sued as a fiduciary of another entity designated simply the "Unitron Graphics, Inc. Profit Sharing Trust," from which Zucker and Fertig also embezzled money. It does not appear that this trust is relevant to this action.

entered into with Mutual Benefit. Under the Contract, Mutual Benefit offered participants in the Plan a choice of five different investment accounts and an option to purchase life insurance. Participants were free to allocate the money in their individual accounts among these six options, but could not choose any other investment options.

On July 1, 1991, Zucker wrote to Mutual Benefit. His letter, in pertinent part, read as follows:

> This is to inform you that we are discontinuing the 401(k) Contract. Please make the necessary arrangements for termination.
>
> I understand that all outstanding expenses owed to Mutual Benefit Life . . . must be remitted to MBL before the distribution can be made. Please make the distribution payable to the company in a lump sum payout and a complete breakdown for each participant to be included.

Pl. Ex. K; Mutual Benefit Ex. 4. The letter was on Unitron stationary, and was signed by Zucker, in his capacity as trustee.

Zucker wrote to Mutual Benefit again on August 15, 1991, requesting release of the Plan funds in four of the six investment accounts, along with a breakdown of the funds by participant. That letter requested Mutual Benefit to make the payment by check payable to the Unitron Graphics, Inc. Profit Sharing Trust. Pl. Ex. L; Mutual Benefit Ex. 5.

After receiving this second letter, Mutual Benefit liquidated the relevant accounts and issued a check in the amount of

$239,811.28 to the order of Unitron Graphics Inc. Profit Sharing Trust. Pl. Ex. P.; Mutual Benefit Ex. 7. The check requisition was signed by defendant Gorny, an employee of Mutual Benefit. It was deposited in the Plan's account at Citibank, N.A. Zucker and Fertig subsequently transferred $109,811.28 of that sum to defendant Principal Mutual Life Insurance Co. ("Principal"), which thereafter managed the Plan's assets. They embezzled the remaining $130,000.

Zucker and Fertig subsequently pled guilty to conspiracy to embezzle funds, in violation of 18 U.S.C. § 371. As part of their sentence, they were ordered to make restitution. Plaintiff was appointed as an independent fiduciary of the Plan by Judge Glasser of this court on November 27, 1994.

Plaintiff commenced this action on February 3, 1995, against Mutual Benefit, Principal, Zucker and Fertig, and subsequently amended the complaint to add Gorny as a defendant. Plaintiff does not seek any relief against Zucker and Fertig beyond the relief already granted in the criminal proceeding. As to the other defendants, however, plaintiff seeks to recover that portion of the $289,811.28 payment embezzled by Zucker and Fertig that he has not been able to recover, plus interest, attorney's fees, and other expenses.[2] Plaintiff contends that these defendants were fiduciaries of the Plan under ERISA, and that they breached their

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2. Plaintiff claims that Zucker and Fertig embezzled a total of $782,105.25 from both the union and non-union divisions of the Plan and from a third trust fund. *See* discussion *supra* note 1. The only money that is at issue in this action, however, is the $289,811.28 that Mutual Benefit transferred to the trustees. Furthermore, plaintiff acknowledges that only $130,000 of that sum was actually embezzled. In addition, he acknowledges that Fertig has made partial restitution of $50,000, and states that he has recovered an additional $141,399.44, some portion of which may be credited toward the funds at issue in this action.

fiduciary duty to the Plan and consequently became liable for its losses.

DISCUSSION

As noted above, the parties to this motion do not disagree as to the underlying facts of this action. Rather, they disagree as to the legal effect that ERISA and the various documents relating to the Plan and the Contract have on the parties. Since there is no genuine issue of material fact, summary judgment is appropriate. *See* Fed.R.Civ.P. 56(c); *see also Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986). The court concludes that, on the undisputed facts of this action, Mutual Benefit and Gorny are entitled to judgment as a matter of law.

I. *Burford* Abstention

At the outset, Mutual Benefit and Gorny urge the court to abstain from deciding the claims against them under the doctrine of *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943). They note that the New Jersey Superior Court placed Mutual Benefit into rehabilitation in July, 1991, and appointed the New Jersey commissioner of insurance as rehabilitator. Under an order of the New Jersey court, all claims against Mutual Benefit had to be filed with the rehabilitator by November 16, 1992. Mutual Benefit and Gorny argue that, under *Burford*, the proper procedure for plaintiff to follow is to file a motion before the New Jersey court to allow late filing of his claim. The court finds this argument unpersuasive, and rejects the contention that abstention is appropriate in this case.

As summarized by the Supreme Court, the *Burford* abstention doctrine provides that:

Appendix B

> Where timely and adequate state-court review is available, a federal court sitting in equity must decline to interfere with the proceedings or orders of state administrative agencies: (1) when there are "difficult questions of state law bearing on policy problems of substantial public import whose importance transcends the result in the case then at bar"; or (2) where the "exercise of federal review of the question in a case and in similar cases would be disruptive of state efforts to establish a coherent policy with respect to a matter of substantial public concern."

New Orleans Public Service, Inc. v. Council of the City of New Orleans, 491 U.S. 350, 361 (1989) (quoting *Colorado River Water Conservation District v. United States*, 424 U.S. 800, 814 (1976)). In general, *Burford* abstention is appropriate "only when a district court is asked to grant equitable relief." *Tribune Co. v. Abiola*, 66 F.3d 12, 18 (2d Cir. 1995); *see also Garamendi v. Allstate Insurance Co.*, 47 F.3d 350, 354 (9th Cir.) (holding that *Burford* abstention does not apply to suits seeking solely legal relief), *cert. granted*, 116 S.Ct. 334 (1995). That in itself suggests that where, as here, the primary remedy that plaintiff seeks is damages, the court should not ordinarily abstain under *Burford*.

In any case, the existence of an alternative forum in the state courts for a timely and adequate review of the plaintiffs claim is a fundamental prerequisite for *Burford* abstention. That distinguishes this case from *Wolfson v. Mutual Benefit Life Insurance Co.*, 51 F.3d 141 (8th Cir. 1995), on which Mutual Benefit and Gorny primarily rely. In *Wolfson*, the plaintiff was a beneficiary of a group life insurance policy issued by Mutual Benefit, and she brought suit under § 502(a)(1)(B) of ERISA to recover her benefits. ERISA explicitly provides that state courts and federal district courts shall have concurrent jurisdiction of

such claims. *See* 29 U.S.C. § 1132(e)(1). The plaintiff in this case is a fiduciary suing under § 502(a)(2) of ERISA, 29 U.S.C. § 1132(a)(2), to recover for an alleged breach of fiduciary duty. ERISA provides for exclusive jurisdiction in the federal district courts over this type of claim. *See* 29 U.S.C. § 1132(e)(1). Therefore, by specific direction of Congress, the New Jersey courts are barred from adjudicating this claim. Since plaintiff cannot raise this claim in the state courts, abstention is inappropriate. *See Levy v. Lewis*, 635 F.2d 960, 967 (2d Cir. 1980) (finding abstention inappropriate where plaintiff seeks to recover for breach of fiduciary duty under ERISA because claim is within exclusive jurisdiction of federal courts).

II. The Merits of Plaintiff's Claim

Under § 404(a)(1) of ERISA, 29 U.S.C. § 1104(a)(1), a fiduciary of an employee benefit is subject to several duties. That section provides, in relevant part, that:

> [A] fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and —
>
> **(A)** for the exclusive purpose of:
>
> **(i)** providing benefits to participants and their beneficiaries; and
>
> **(ii)** defraying reasonable expenses of administering the plan;
>
> **(B)** with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a

> like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims; [and]
>
> . . .
>
> **(D)** in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of this subchapter or subchapter III of this chapter.

Any fiduciary who breaches this duty is personally liable to the Plan for any losses resulting from the breach. 29 U.S.C. § 1109. The gravamen of this action is that in closing the Plan's accounts and paying its money over to the trustees, Mutual Benefit and Gorny were acting as fiduciaries and breached their duty to the Plan by failing to act with reasonable care.

Section 402(a)(1) of ERISA, 29 U.S.C. § 1102(a)(1), provides that all employee benefit plans must be established pursuant to a written instrument that "provide[s] for one or more named fiduciaries who jointly or severally shall have authority to control or manage the operation and administration of the plan." In this case, the written instrument that established the Plan clearly stated "[t]he 'named fiduciaries of this Plan are (1) the Employer [Unitron], (2) the Trustees [Zucker and Fertig], and (3) the Plan Administrator [also Unitron]." Pl. Ex. F, at 23,

Neither Mutual Benefit nor Gorny was a named fiduciary of the Plan.[3] That fact, however, does not mean that they did not

3. Plaintiff argues that Zucker and Fertig were not fiduciaries of the Plan, and that Mutual Benefit therefore must have been a fiduciary. That argument is plainly without merit. The provision of the Plan that plaintiff points to states that: (Cont'd)

have fiduciary duties under ERISA. Indeed, § 3(21)(A) of ERISA expressly provides that:

> a person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.

29 U.S.C. § 1002(21)(A). Thus a person May be a "fiduciary" with respect to a plan when carrying out certain activities, and yet not be a fiduciary when performing other activities. *See Johnson v. Georgia-Pacific Corp*, 19 F.3d 1184, 1188 (7th Cir. 1994) ("[T]his definition does not make a person who is a fiduciary for one purpose."); *Kerns v. Benefit Trust Life Ins.*

(Cont'd)

> Participants may choose among the Investment Accounts defined in the Contract as selected by the Employer, change their choices and transfer between Investment Accounts, as permitted in the Contract. The Participant's choice of Investment Accounts relieves the Trustee(s) of fiduciary responsibility.

Pl. Ex. F, at 11. This language cannot reasonably be interpreted to mean that Zucker and Fertig were not fiduciaries. It simply means that Trustees could not be held responsible for a participant's decision to place his Plan assets in one investment account as opposed to another. *See* 29 U.S.C. § 1104(c)(2) (providing that, in individual account plan, fiduciaries are not liable for loss that results from participant or beneficiary's exercise of control).

Co., 992 F.2d 214, 217 (8th Cir. 1993) ("Fiduciary status under § 1002(21)(A) is not an all-or-nothing concept.") (internal quotation marks and citation omitted); *see also Varity Corp. v. Howe*, 116 S.Ct. 1065, 1071 (1996) (noting that person is subject to fiduciary duties to the extent of statutory definition).

Mutual Benefit and Gorny go to great lengths to argue that they were not fiduciaries of the Plan under ERISA. These arguments are somewhat misplaced. Under the functional definition of § 3(21), it is clear that Mutual Benefit, at least, was a fiduciary of the plan, in that it exercised control over the management of the Plan's assets. Furthermore, even after its contract to manage the assets was terminated, it remained a fiduciary as long as those assets remained in its possession, and hence under its control, albeit nondiscretionary. In the language of the statute, Mutual Benefit continued to "exercise[ ] authority or control respecting . . . disposition of [the Plan's] assets." 29 U.S.C. § 1002(21)(A).

Under the terms of the Contract, however, once the trustees made a request for the release of the Plan's funds, Mutual Benefit had no authority to refuse it. The language of the contract governing discontinuance provides, in relevant part:

> **DISCONTINUANCE**
>
> You [the trustees] may discontinue this contract at any time by notifying us in writing. The date we receive the notice will be the discontinuance date.
>
> This contract is automatically discontinued if the Plan is terminated.
>
> . . .

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EFFECT OF DISCONTINUANCE
Discontinuance will not affect payment of any annuities purchased under this contract.

If the contract discontinues for reasons other than Plan termination, Investment Accounts held under this contract will be paid to you, after deduction of any unpaid expenses, outstanding loans, and accrued interest . . . .

Pl. Ex. E, at 26. Zucker's letter of July 1, 1991 clearly indicated that the trustees were discontinuing the Contract, as they were entitled to do. The terms of the Contract therefore required Mutual Benefit to pay the investment accounts over to the trustees.

It is unclear from the record why Mutual Benefit did not immediately liquidate the Plan's accounts and pay them over to the trustees. Mutual Benefit and Gorny note that the original letter requested distribution to the "company," and that the contract authorized distribution only to the trustees. Defs. Mem. in Opp. at 8. The contention that this improper designation caused the delay is neither supported nor contradicted by anything else in the record, however. It is also true that the contract does not explicitly authorize the partial release of funds, as requested in Zucker's letter of August 15, 1991. Gorny's deposition testimony makes it plain, however, that at the time of Zucker's request, Mutual Benefit was under court-supervised rehabilitation, and no funds could be withdrawn from the fixed income account. Pl. Ex. O, at 41-42. Zucker's request sought the release of the Plan funds in the four remaining accounts. Under the terms of the Contract, Mutual Benefit — and Gorny, its employee — were clearly obligated to comply with that request.

Plaintiff contends that, because the letters were signed by only one trustee, Zucker, Mutual Benefit and Gorny should have suspected that something was amiss. Even leaving aside the fact that the co-trustee, Fertig, was also involved in the subsequent embezzlement, this argument is unpersuasive. As Mutual Benefit and Gorny note, the written agreement establishing the Plan specifically provided that "[t]he Insurer [Mutual Benefit] may rely on the signature of any Trustee on an application for or any document used in connection with a Contract or Policy." Pl. Ex. F, at 24. As fiduciaries, Mutual Benefit and Gorny were required to discharge their duties in accordance with the written terms of the plan. *See* 29 U.S.C. § 1104(a)(1)(D). Furthermore, the Contract between the Trustees and Mutual Benefit provided that:

> We [Mutual Benefit] are entitled to assume that the Plan permits any action taken by you [the trustees]. We are not a party to the Plan, and are not responsible for its validity. Except as expressly provided in this contract or any other written agreement accepting responsibility, we are not responsible for any duties under the Plan or for any duties of the Plan administrator or named fiduciary.
>
> We may rely on any action taken by you under this contract, and will be held harmless and completely discharged when acting on your direction or authorization.

Pl. Ex. E, at 23. In light of these specific provisions in the Plan and the Contract, it was reasonable for Mutual Benefit and Gorny to rely on the signature of one trustee to release the funds.

Plaintiff's argument that, under ERISA, a single trustee has no authority to order the release of funds stems from a misreading

of the Seventh Circuit's decisions in *Illinois Conference of Teamsters and Employers Welfare Fund v. Mrowicki*, 44 F.3d 451 (7th Cir. 1994) and *Mason & Dixon Lines v. Glover*, 975 F.2d 1298 (7th Cir. 1992). In *Glover*, an employer brought suit against an ERISA pension fund seeking specific performance of an alleged agreement to settle a lawsuit. One of the plan's four trustees had orally stated that the settlement was a "done deal"; the plan and the trustees argued that a single trustee did not have either actual or apparent authority to enter into a settlement on behalf of the fund. *Id.* at 1302. The Seventh Circuit agreed. With respect to the issue of actual authority, it noted that § 405(b)(1)(B) of ERISA, 29 U.S.C. 1105(b)(1)(B), provides that, where the assets of a fund are held by two or more trustees, the trustees must "jointly manage and control the assets of the plan. . . ." 975 F.2d at 1303. It then looked to the common law of trusts for guidance, noting that the exercise of joint powers requires the action of all trustees. *Id.*; *see also Restatement (Second) of Trusts* § 194 (1959) ("If there are two or more trustees, the powers conferred upon them can properly be exercised only by all the trustees, unless it is otherwise provided by the terms of the trust."). Because the other trustees had not consented, the court concluded that the trustee who made the oral representation at issue did not have actual authority. 975 F.2d at 1303. It noted, however, that the plan might still have been bound if the trustee had apparent authority to enter into a settlement agreement on behalf of the trustees. *Id.*

In *Mrowicki*, the court essentially summarized and restated its holding in *Glover*. The relevant issue in that case was whether statements made by a plan trustee excused an employer's obligation to make contributions to the plan. 44 F.3d at 462. After reiterating its analysis in *Glover*, the court found that, at the time the statements were made, the speaker was not a trustee, and he therefore lacked both actual and apparent authority. *Id.* at 463.

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Nothing in *Glover* or *Mrowicki* suggests that an investment manager such as Mutual Benefit cannot rely on the signature of a single trustee to release funds where the Plan instrument expressly authorizes such action. Indeed, both *Glover* and *Mrowicki* recognize that, under ERISA, as at common law, trustees may delegate authority to an agent to perform certain acts. 975 F.2d at 1303; 44 F.3d at 463. Furthermore, it is quite clear that the common law rule on which *Glover* relied is simply a default provision that can be changed by the terms of a trust. *See Restatement (Second) of Trusts* § 194 cmt. d (1959) ('[B]y the terms of the trust the trustees may be permitted to delegate to one or more of their number the exercise of powers"). ERISA carries forward this rule by providing that, where authorized by the trust instrument, trustees may enter into an agreement allocating specific responsibilities, duties, or obligations among themselves.

Plaintiff correctly notes that the Plan in this case provided that:

> If more than one person is serving as Trustee, they shall act by a majority of their number but may authorize one or more of them to sign all papers on their behalf.

Pl. Ex. F, at 26. He argues that because Zucker, on his own, did not constitute a majority of the trustees, and because plaintiffs have not produced any evidence that Fertig actually did authorize Zucker to sign papers on behalf of the trust, Mutual Benefit could not rely on a single trustee's signature. This argument overlooks the fact that the Plan specifically authorized Mutual Benefit to act on the basis of one trustee's signature. Thus, even if plaintiff could show that Zucker's action was not authorized by the second trustee, it would not follow that Mutual Benefit acted improperly

in complying with Zucker's instruction. The court concludes that Mutual Benefit's action in releasing the funds to the trustees was authorized by the Plan and the Contract.

Plaintiff also argues that the language of the summary plan description ("SPD") distributed to Unitron employees, rather than the language of the Plan agreement itself, should govern here. This argument is without merit. It is true that the Second Circuit has held that where the written instrument that establishes a plan *conflicts* with a plan summary, the summary should govern. *Heidgerd v. Olin Corp.*, 906 F.2d 903, 907-08 (2d Cir. 1990). Plaintiff has not identified any such conflict here, however. The fact that the SPD does not outline the specific procedures that the trustees and Mutual Benefit would follow in the event the Contract was discontinued does not mean that those procedures are invalid. As defendants correctly note, "it is not necessary for a plan summary to restate each term of a benefit plan because such a requirement would defeat the summary's clear purpose of providing a clear and concise description of the employees' rights and obligations under the plan." *Sansevera v. E. I. DuPont de Nemours & Co.*, 859 F. Supp. 106, 112 (S.D.N.Y. 1994). Here, the SPD does state that Unitron has the right to amend or discontinue the Plan. Pl. Ex. G, at 9. That language was sufficient to alert participants to the possibility that the trustees might discontinue the contract with Mutual Benefit and invest the Plan's assets elsewhere. The SPD does not purport to describe the procedures to be followed by the trustees in the event they decided to take such action, nor would it be logical to expect a "concise description of the employees' rights and obligations" to contain such details.

Plaintiffs reliance on *In re Unisys Savings Plan Litigation*, 74 F.3d 420 (3d Cir. 1996), is similarly unavailing. In that case,

the plaintiffs argued that Unisys, the plan administrator, had breached its fiduciary duty by, among other things, making misrepresentations concerning the nature of and risks associated with investments in certain fixed income accounts in an individual account plan similar to that at issue here. The court reiterated its previously expressed position that ERISA imposes a duty on a plan administrator not to mislead participants or beneficiaries either by affirmative misrepresentations or material omissions. Even assuming that the statements in the SPD are attributable to Mutual Benefit and Gorny, plaintiff has not identified any affirmative misrepresentation in the SPD. Furthermore, as previously discussed, nothing in ERISA requires an SPD to state every detail of a plan. In fact, doing so would tend to defeat the purpose of the SPD. *See* 29 U.S.C. § 1022 (describing information that must be included in SPD). Procedural details, such as the number of trustees who must consent to a transaction, or the precise procedure to be followed in the event a group annuity contract is discontinued, are appropriately omitted from such a plan summary.

In sum, the evidence submitted to the court establishes that, as a matter of law, Mutual Benefit and Gorny did not breach a fiduciary duty to the Plan by releasing to the trustees the funds that are the subject of this action. Summary judgment for these defendants is therefore appropriate.

CONCLUSION

For the foregoing reasons, plaintiffs motion for summary judgment is denied and Mutual Benefit and Gorny's motion for summary judgment is granted.

SO ORDERED.

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s/ Allyne R. Ross
Allyne R. Ross
United States District Judge

Dated: April 19, 1996
Brooklyn, New York

APPENDIX C — OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF NEW YORK DATED MAY 16, 1996

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

95-CV-0500 (ARR)

David W. SILVERMAN

Plaintiff,

-against-

MUTUAL BENEFIT LIFE INSURANCE CO. et al.

Defendants.

OPINION AND ORDER

ROSS, United States District Judge:

In this action, a court-appointed fiduciary of an employee benefit plan seeks to hold an insurance company that acted as the plan's investment manager liable for the theft of assets by the plan's trustees. Plaintiff, David Silverman, argues that the insurance company, defendant Principal Mutual Life Insurance Co. ("Principal"), is liable as a co-fiduciary for the actions of the trustees under § 405(a) of the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. § 1105(a). Principal and plaintiff have cross-moved for summary judgment. For the reasons stated herein, Principal's motion is granted, and plaintiff's motion is denied.

Appendix C

FACTUAL BACKGROUND

Many of the facts relating to this action were outlined in the court's opinion and order of April 19, 1996, granting summary judgment for defendants Mutual Benefit Life Insurance Co. ("Mutual Benefit") and Helene Gorny, and dismissing plaintiff's claims against them. On July 15, 1988, Unitron Graphics, Inc. ("Unitron Graphics") established two profit-sharing plans (collectively, the "Plan") for the benefit of its employees.[1] Zucker and Fertig, both officers of Unitron Graphics, were the trustees of the Plan and the named fiduciaries pursuant to § 402 of ERISA, 29 U.S.C. § 1102.

The Plan was what is known under ERISA as an "individual account plan" or a "defined contribution plan." *See* 29 U.S.C. § 1002(34). Each participating employee could elect to have Unitron set aside part of his salary and contribute it to the Plan. In addition, the company could make matching contributions and discretionary contributions. Prior to July 1, 1991, the Plan's assets were invested in a group annuity contract with Mutual Benefit. That contract provided that Mutual Benefit would maintain a separate account for each participant in the plan, and allowed

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1. The two plans were identical, except that one was established for the benefit of union employees and one for the benefit of non-union employees. Plaintiff has sued as a fiduciary of the "Unitron Graphics, Inc., Profit Sharing Trust—Union and Non-Union Divisions," essentially treating both trusts as a single entity. Since the distinction between the two plans is not material for the purposes of the issues presented here, the court will also treat the two plans as a single entity.

Plaintiff has also sued as a fiduciary or of another entity designated simply the "Unitron Graphics, Inc. Profit Sharing Trust," from which Zucker and Fertig also embezzled money. It does not appear that this trust is relevant to this action.

each participant to allocate the money in his account among several different investment accounts that Mutual Benefit offered.

On July 1, 1991, Zucker wrote to Mutual Benefit and discontinued the Plan's group annuity contract. On that same day, he and Fertig entered into two new group annuity contracts with defendant Principal. Like the contract with Mutual Benefit, the contracts with Principal offered participants a choice of several investment options, and provided for individual recordkeeping for each participant's account. They also explicitly provided that:

> Application for and issuance of this contract constitutes appointment of and acceptance and affirmation by us [Principal] that (i) we are an Investment Manager as described under [ERISA] with respect to Plan assets held under this contract . . . and (ii) we are qualified to accept such appointment and acknowledge that by virtue of such appointment we are a fiduciary of the Plan, within the meaning of [ERISA] with respect to our responsibilities as Investment Manager.

Saunders Aff., Ex. A, at 241; Saunders Aff. Ex B, at 298. The contracts did not specify that Principal was to be the sole investment manager of the Plan's assets. They did, however, set forth explicit procedures that the trustees were to follow in the event they decided to transfer any of the Plan's assets to an "alternate funding agent." Saunders Aff., Ex. A, at 235; Saunders Aff. Ex B, at 292.

For reasons that are not entirely clear, Mutual Benefit did not release the Plan's funds immediately after Zucker's letter of July 1, 1991. On August 15, 1991, Zucker again wrote to Mutual

Benefit, requesting release of certain of the funds held in certain of Mutual Benefit's investment accounts.[2] On August 30, 1991, Mutual Benefit issued a check made payable to the order of the Unitron Graphics, Inc. Profit Sharing Trust in the amount of $239,811.28. That check was deposited in the Plan's bank account at Citibank, N.A., on September 6, 1991.

Between September 20 and October 8, 1991, Zucker and Fertig embezzled $130,000 from the Plan by drawing three checks on the Citibank account. Two of the three checks were made payable to Zucker, and the third was made payable to his son. All three checks were signed by Zucker. *See* Wolfson Aff. Ex. D. The balance of the payment from Mutual Benefit, $109,811.28, was forwarded to Principal by wire transfer on October 8, 1991.

Prior to receipt of this money, Principal had received a letter from Howard Lowett, vice president for administration at Unitron Graphics, enclosing a breakdown by participant of the money that the Plan had received from Mutual Benefit. That letter, dated September 17, 1991, clearly indicated that the total sum Mutual Benefit had sent the trustees was $239,811.28. Consequently, Principal knew by October 8, 1991, the date on which it received the wire transfer, that it did not have all of the Plan's assets. Furthermore, Principal was unable to allocate the $109,811.28 that it did have among the plan participants, because it had no way of knowing how to account for the missing $130,000 reflected on the statement from Mutual Benefit. Accordingly, Principal placed the entire sum in a money market account, where it would earn interest.

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2. As discussed in the court's opinion and order of April 19, 1996, Mutual Benefit was under a rehabilitation order from the New Jersey Superior court at the time of Zucker's request, and all funds in fixed-income accounts had been frozen. Zucker's letter requested the release of the remaining funds.

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On November 5, 1991, Principal wrote to Zucker and Fertig. That letter raised two concerns that Principal had about the Plan. First, it noted that, with the exception of one payment, Principal had not received any of salary deferral contributions that Unitron was required to make to the Plan. Pursuant to a Department of Labor ("DOL") regulation, such salary deferrals become part of a plan's assets no later than 90 days after they are withheld from an employee's paycheck. *See* 29 C.F.R. § 2510.3-102 (1989). Second, it inquired about the missing $130,000. The letter stated, in relevant part:

> [W]e have learned that Mutual Benefit . . . has liquidated and transferred to the Plans' Trustees all separate account assets that had been held by them. In turn, we have received, from what limited recordkeeping data we have, only a portion of those separate account assets. The balance of these assets must be accounted for. It is our understanding that we are to be the only investment manager for your profit sharing plans. Given this, please forward the balance of these funds.
>
> If you have no intention of forwarding these funds in their entirety to us, contact us immediately in writing via the FAX number indicated below. On that basis, we will need to make an internal decision on whether we can continue to be associated with the Unitron Graphics, Inc. Profit Sharing Plans.

Saunders Aff. Ex. G; Pl. Ex. 6. Zucker and Fertig did not reply to this letter.

Principal did not take any further immediate action. Several internal memoranda submitted by plaintiff, however, disclose that

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Principal was aware of a potential legal problem with respect to the Plan. For example, one such memorandum, written by Marla Gowdey, an assistant analyst with Principal, and dated November 13, 1991, reads:

> Spoke to John Lee on 11/13/91. He told me that there may be a legal issue/problem on this case. We discussed that I probably should not call the client about anything until I hear from him.
>
> The client has received $130,000 transfer money from Mutual Benefit and is holding on to it instead of submitting it to us. They also have not been submitting regular contributions to us. The group rep and legal department are involved and a letter has been sent to the client requesting immediate deposit of funds.

Pl. Ex. 9. Two memoranda also indicate that, on January 14, 1992, a participant in the Plan named Lance Burt called Gowdey to request information about his account.

On January 28, 1992, Principal, through its assistant counsel, Randy Bolin, wrote again to Zucker and Fertig. The second letter reiterated the points made in the first letter in somewhat stronger language:

> To date we have received no response to [the November 5] letter. Your failure either to forward the requested funds to us or to notify us in writing of your intention not to forward these funds has forced us once again to address these issues with you.
>
> . . . .

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. . . We have learned that Mutual Benefit recently transferred these separate account assets to you in your capacity as the plan trustees. Our records indicate, however, that we have only received a portion of these separate account assets from you since their release by Mutual Benefit. The balance of these assets must be accounted for. Within five business days after receipt of this letter, we request that you forward to us the balance of the separate account assets that were released to you by Mutual Benefit.

It continues to be our understanding that we are to be the only investment manager for your profit sharing plans. If this understanding is incorrect, we request that you notify us of this fact in writing within five business days after receipt of this letter. In addition we request that you notify us of the name or names of the outside investment managers that you intend to utilize in connection with your profit sharing plans and the amount of assets that have been transferred by you to these investment managers.

If you have no intention of forwarding the requested funds in their entirety to us within five business days, please contact me immediately in writing via the FAX number indicated below. If we do not receive the requested funds from you, or a written response indicating your intended actions with respect to these funds within five business days after your receipt of this letter, we will be forced to provide you with the required written notice pursuant to our contracts that we will refuse any further contributions from you under the contracts.

Bolin Aff. Ex. A; Pl. Ex. 12.

Bolin's letter also addressed the delinquent contributions that Unitron was required to make to the Plan. With respect to that issue, he wrote:

> [I]t is our opinion that Section 502(*l*) of [ERISA] will require us to notify the Secretary of Labor of the fact that, according to our records, you do not appear to be currently complying with the requirements of DOL regulation 2510.3-102 in connection with the operation of your 401(k) plans. Under § 502(*l*) of ERISA, the Secretary of Labor has the authority to assess a 20% penalty against any fiduciary who breaches his or her fiduciary duty or against any other person who knowingly participates in such a breach. . . .
>
> Knowledge of your apparent failure to comply with Regulation 2510.3-102 subjects Principal Mutual Life Insurance Company to potential penalties under Section 502(*l*) of ERISA if we do not act reasonably and in good faith. It is our opinion that to allow the current situation with respect to the employee deferrals to your 401(k) plans to exist any longer would not be held by the Secretary of Labor to be an action taken by us that was reasonable and in good faith.

Bolin Aff., Ex. A; Pl. Ex. 12.

In spite of these stem warnings, Zucker and Fertig again failed to respond. Shortly after the second letter was written, however, an individual named "Mr. Freilich" contacted Bolin. He informed Bolin that Unitron Graphics had filed for bankruptcy, and asked if Principal would be willing to delay any notification to the Department of Labor for twelve months, until a buyer could

be found for the company. Bolin stated in a memorandum, and reaffirmed in an affidavit to the court, that he told Freilich that Principal could not agree to such a request under any circumstances. Pl. Ex. 14; Bolin Aff. ¶ 5.

Nonetheless, Principal did not notify the Department of Labor or take any other formal action. Internal memoranda written in the wake of Bolin's letter again indicate Principal's awareness of a significant problem. One memorandum, written by Gowdey and dated February 13, 1992, reads:

> This company [Unitron Graphics] has filed Chapter 11. Also, the trustees have been withholding payments to the retirement plans. Mike Saunders is the group rep and became aware that the trustees were not living up to their fiduciary responsibilities. Randy Bolin from Legal has been involved.
>
> John Lee, Randy Bolin, and Scott Einck have been working very closely on the situation. Letters have been sent to the client. The last letter threatened that we were going to contact the DOL. It sounds as if some of the employees (a union is involved) have already contacted the DOL, so we may not need to contact them in our name.

Pl. Ex. 13.

In fact, Principal did not take any further action until March 30, 1992. On that date, the Department of Labor wrote to Principal, requesting information relating to the delinquent contributions and the funds from Mutual Benefit. Principal promptly complied with the DOL's request by letter dated April 2, 1992, and included copies of the November 5 and January 28 letters.

Zucker and Fertig were subsequently indicted on charges of embezzlement, conspiracy to embezzle, bank fraud, and filing false documents with the Internal Revenue Service. The allegations in the indictment reached well beyond the specific transactions that are at issue in this action; it charged that Zucker and Fertig had embezzled hundreds of thousands of dollars from the 401(k) plans and a third trust fund. Zucker and Fertig pled guilty to conspiracy to embezzle funds, in violation of 18 U.S.C. § 371. Judge Glasser of this court ordered the two men to make restitution, and appointed plaintiff as an independent fiduciary to collect all funds owed to the plans.

Plaintiff subsequently commenced this action against Principal, Mutual Benefit, Zucker and Fertig, seeking to recover the $130,000 embezzled by Zucker and Fertig. He subsequently amended the complaint to add a Mutual Benefit employee, Helene Gorny, as a defendant. In an opinion and order dated April 19, 1996, this court dismissed plaintiff's claims against Mutual Benefit and Gorny. Since plaintiff does not seek any relief against Zucker and Fertig beyond that already granted in the criminal proceeding, the only substantive claims that remain are those against Principal.

DISCUSSION

Summary judgment is appropriate when no genuine issue of material fact exists in an action, and the moving party is entitled to judgment as a matter of law. *See* Fed.R.Civ.P. 56(c); *see also Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986). In this case, the parties do not dispute most of the basic facts underlying this action. Rather, their dispute primarily involves questions of law, including the nature and scope of Principal's responsibilities as a fiduciary under ERISA. Summary judgment is therefore appropriate.

Appendix C

I. Jurisdiction

The court begins its analysis by addressing an issue not raised by either party in its papers: subject-matter jurisdiction. Federal courts are all courts of limited jurisdiction, and the existence of a valid basis of jurisdiction is a threshold question in every federal case. In this case, plaintiff has identified § 502 of ERISA, 29 U.S.C. § 1132, and the general federal question jurisdiction statute, 28 U.S.C. § 1331, as authorizing jurisdiction in this action. The court agrees that it has jurisdiction over this matter. Some discussion of the reasoning behind that conclusion, however, is appropriate, because it helps to clarify an important legal issue in this case: whether plaintiff must prove that Principal's conduct actually caused the loss to Plan.

Section 502(a) of ERISA, as amended, lists nine different types of civil actions that may be brought under ERISA, three of which may be brought by fiduciaries of a plan. The relevant provisions of § 502(a) read as follows:

> **(a) Persons empowered to bring a civil action**
>
> A civil action may be brought —
>
> . . . .
>
> (2) by the Secretary [of Labor], or by a participant, beneficiary or fiduciary for appropriate relief under section 1109 of this title; [or]
>
> (3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any

> provision of this subchapter or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provision of this subchapter or the terms of the plan. . . .

29 U.S.C. § 1132(a). Section 502(e)(1) provides for exclusive jurisdiction in the federal district courts over both these types of action. In this case, plaintiff does not explicitly claim that he is seeking relief against Principal under § 409 of ERISA, 29 U.S.C. § 1109, which provides that "[a]ny person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan resulting from each such breach. . . ." 29 U.S.C. § 1109(a). Rather, he hinges his claims against Principal solely on § 405(a) of ERISA, 29 U.S.C. § 1105(a), which describes the circumstances under which a fiduciary may be held liable for his co-fiduciary's breach of duty.

On its face, § 405 appears to provide a basis for imposing liability on a co-fiduciary that is independent from § 409. The caption of § 405 reads, "Liability for breach of cofiduciary" — language that appears to parallel the caption of § 409, "Liability for breach of fiduciary duty." Furthermore, the first sentence of § 405(a) provides that a fiduciary's liability for a co-fiduciary's breach in the enumerated circumstances will be "[i]n addition to any liability which he may have under any other provision of this part. . . ." These factors tend to suggest that Congress intended § 405 and § 409 to provide alternative, independent bases for imposing liability on fiduciaries.

That impression is belied, however, by an examination of ERISA's jurisdictional provisions in § 502. Although Congress

authorized several types of plaintiffs to sue for violations of § 409, it did not create a parallel provision directly authorizing suits under § 405. As a fiduciary, plaintiff's options are limited to the types of suits described in § 502(a)(2) and (3). Furthermore, it is clear that § 502(a)(3) cannot authorize this action with respect to Principal. Plaintiff is not seeking to enjoin any act or practice or to enforce a provision of ERISA or the Plan. Nor is he seeking "other appropriate equitable relief" within the meaning of the statute. Plaintiff is seeking money damages from Principal as a result of Zucker and Fertig's breach. Although money damages were available from courts of equity at common law, the Supreme Court has made it clear that such damages are not "equitable relief" authorized by § 502(a)(3).[3] *See Mertens v. Hewitt Associates*, 113 S.Ct. 2063, 2069 (1993).

For this action to be cognizable under ERISA, it must be an action under § 502(a)(2) for appropriate relief under § 409, since § 405 does not provide an independent basis of liability. It simply imposes special duties that govern a fiduciary's relationship to its co-fiduciaries.[4] Consequently, plaintiff must meet the

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3. As a alternative to money damages, plaintiff seeks restitution, which is a form of "equitable relief" authorized by § 502(a)(3). *See Mertens*, 113 S.Ct. at 2068, 2069. Since there is no allegation here that Principal itself took any money from the Plan or otherwise profited from the trustees' misconduct, the remedy of restitution is unavailable.

4. In rare circumstances, courts have also recognized federal common-law rights of action under ERISA that do not fall into any of the categories enumerated in § 502(a). For example, the Second Circuit has recognized a common-law right of action by participants against non-fiduciaries for knowing participation in a breach of fiduciary duty. *Diduck v. Kaszycki & Sons Contractors*, 974 F.2d 270, 280-81 (2d Cir. 1992). Courts must undertake such projects with care, since ERISA's "carefully crafted and detailed enforcement

(Cont'd)

requirements of § 409 as well as the requirements of § 405 to prevail in this action. In order to prevail, then, plaintiff must prove (1) that Principal is a fiduciary, (2) that Principal breached a fiduciary duty imposed by § 405, and (3) losses to the Plan resulting from such breach. Each of these elements is discussed below.

II. Principal's fiduciary status

To be liable under either § 409 or § 405, a defendant must be a "fiduciary" of an ERISA plan. Principal acknowledges that it was a fiduciary under ERISA for certain purposes, but contends that its duties were limited to the prudent management of the funds that it actually received from Zucker and Fertig. Since plaintiff does not argue that Principal engaged in any misconduct with respect to those funds, Principal contends that it is immune from liability for breach of fiduciary duty.

The court rejects this contention. Under § 3(21)(A) of ERISA:

> a person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation,

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(Cont'd)
scheme provides 'strong evidence that Congress did not intend to authorize other remedies that it simply forgot to incorporate expressly.' " *Mertens*, 113 S.Ct. at 2063 (quoting *Massachusetts Mutual Life Insurance Co. v. Russell*, 473 U.S. 134, 146-47 (1985)). Since § 502(a)(2) provides a vehicle for enforcing § 405, the court is unwilling to infer the existence of a direct federal common law action under § 405 and 28 U.S.C. § 1331.

> direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.

29 U.S.C. § 1002(21)(A). Here, the group annuity contracts between the trustees and Principal specifically appointed Principal as an investment manager and acknowledged that it was a fiduciary. Moreover, Principal's November 5 and January 28 letters to the trustees indicate that Principal understood that it was to be the Plan's sole investment manager. If Principal was appointed as the sole investment manager of the Plan, with authority and control over the management of its assets, then it had a fiduciary responsibility with respect to all of those assets, whether or not it actually received them.

The cases Principal cites to the contrary are easily distinguishable. In *Brandt v. Grounds*, 502 F. Supp. 598 (N.D. Ill. 1980), *aff d*, 687 F.2d 895 (7th Cir. 1982), a trustee of an ERISA plan embezzled $175,000 from two bank accounts. The other trustees sued the bank, alleging a breach of fiduciary duty. They argued that the bank was a fiduciary under ERISA because it had provided investment advice for a fee. The district court held, and the Seventh Circuit affirmed, that the bank's fiduciary status was limited to its function as an investment advisor, and that there was no causal connection between the advice that the bank rendered and the trustee's theft. Here, by contrast, Principal's fiduciary status does not depend simply on the fact that it offered investment advice. Rather, it stems from the fact that Principal agreed to be an investment manager with broad responsibility over the management and control of the Plan's assets. If Principal had undertaken to manage only a portion of

the Plan's assets, then it might be immune from liability with respect to the assets that it did not manage. Here, however, Principal's own correspondence indicates that it understood that it was to be the sole manager of the Plan's assets.

Pension Fund—Mid Jersey Trucking Industry—Local 701 v. Omni Funding Group, 731 F. Supp. 161 (D.N.J.) involved a plan whose trustees set up an acquisition fund at a bank for the purpose of investing in mortgage loans. Although the bank had no discretion or control over these investments, it had authority to invest any excess monies from the fund in short-term securities. The court held that the bank was a fiduciary only with respect to the short-term security fund over which it exercised discretionary control. The alleged breach related solely to the mortgage loans. Relying on the district court decision in *Brandt*, the court concluded that the bank could not be liable because there was no causal link between its fiduciary role and the breach of its co-fiduciaries' duties. Again, however, the factual record in this case contains evidence indicating that Principal expressly assumed responsibility for all of the Plan's assets.

Care must be taken at this point to distinguish between two different issues that are somewhat conflated in the *Brandt* and *Omni Funding Group* opinions. The mere fact that Principal had a fiduciary duty with respect to the funds Zucker and Fertig embezzled from the Plan does not mean that the loss to the Plan resulted from a breach of that duty. That issue, also addressed in *Brandt* and *Omni Funding Group*, is dealt with below. Based on Principal's own correspondence, however, the court concludes that, at the least, a genuine issue of material fact remains in this action as to whether Principal was a fiduciary with respect to the funds embezzled by Zucker and Fertig.

III. Principal's liability under § 405(a)

Plaintiff alleges in this action that, as a fiduciary of the Plan, Principal is liable for Zucker and Fertig's breach of their fiduciary duty under § 405(a) of ERISA. That section provides that:

> In addition to any liability which he may have under any other provision of this part, a fiduciary with respect to a plan shall be liable for a breach of fiduciary responsibility with respect to the same plan in the following circumstances:
>
> > (1) if he participates knowingly in, or knowingly undertakes to conceal, an act or omission of such other fiduciary, knowing such act or omission was a breach;
> >
> > (2) if, by his failure to comply with section 1104(a)(1) of this title in the administration of his specific responsibilities which give rise to his status as a fiduciary, he has enabled such other fiduciary to commit a breach; or
> >
> > (3) if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach.

29 U.S.C. § 1105(a). Although the complaint alleges only that Principal is liable under § 405(a)(2) and (3), plaintiff argues in his moving papers that Principal is also liable under § 405(a)(1). The court addresses each of these contentions in turn.

Appendix C

A. Liability under § 405(a)(1)

To hold a fiduciary liable under § 405(a)(1), a plaintiff must show (1) that a cofiduciary breached a duty to the plan, (2) that the fiduciary knowingly participated in the breach or undertook to conceal it, and (3) damages resulting from the breach. *See Diduck v. Kaszcyki & Sons Contracting*, 974 F.2d 270, 281-82 (2d Cir. 1992) (listing elements of analogous cause of action for non-fiduciary's knowing participation in breach of fiduciary duty). In this case, plaintiff does not argue that Principal participated in Zucker and Fertig's theft. Rather, he argues that Principal knowingly attempted to conceal the theft after it had already occurred.

The court finds this argument unpersuasive. At most, the record indicates that Principal failed to act with diligence based on the knowledge that it had. A failure to act with reasonable diligence is not tantamount to concealment, and plaintiff has not identified any evidence that suggests that Principal actively attempted to conceal what it knew about the trustees' conduct. To support his claim of concealment, plaintiff points first to a memorandum, written by Bolin, describing his conversation with Freilich. Although the conversation described in that memorandum appears to involve a request by Freilich that Bolin conceal information from the Department of Labor, Bolin's memorandum and his affidavit both emphatically deny that he ever agreed to this request. Nor has plaintiff pointed to anything in the record that contradicts Bolin's assertion. Plaintiff's assertion that Principal was "less than candid," Pl. Mem. at 14, in its reply to the Department's inquiry is wholly unsupported by the record. Principal responded to the letter dated March 30, 1992, on April 2, 1992, and supplied all of the information that the Department requested, including the two letters that it had sent to the trustees.

Appendix C

Plaintiff also asserts that Principal attempted to mislead the participants in the Plan, or, alternatively, that it failed to disclose material information to them. That argument is based entirely on two internal memoranda describing Gowdey's conversation with Lance Burt, a participant in the Plan. The first of these memoranda, written by Gowdey and dated January 14, 1992, reads as follows:

> I received a call from Lance Burt who is an employee at Unitron Graphics. He said that Howard Lowett [at Unitron Graphics] gave him my name to call and find out about his account. He said that he knows that his money had transferred to us from Mutual Benefit and he was wondering what he had in his account. I told him that I didn't have enough information to allocate the money received to the individuals' accounts, but that he can be assured that his money is earning interest daily. He argued with me that we've had the money since September and I should be able to tell him something. I took his name and number . . . and told him that I had to check with a couple of people and someone would call him back.
>
> (This is the case that the employer has been holding the monies and not submitting them. Our legal department is involved.)
>
> I called John Lee in underwriting. Told him that someone needs to tell Howard Lowett not to have the employees call me and also that someone needs to call Lance Burt back since I have no information to give him. John said he would talk to Linnette Martin in the Group office. One of them would call Howard

> Lowett and tell him not to give my name and number out and they would also tell him to contact Lance Burt.

Pl. Ex. 11. The second memorandum, also dated January 14, 1992 is from John Lee. It states, in relevant part:

> I called Lynn Martin to explain to her that a participant from Unitron called home office to get information on his account, balance, etc. Marla told him that we do not have complete information from the employer for allocations, so we were not able to tell him anything. His name is Lance Burt. . . .
>
> I explained to Lynn that we did not want any call from participants calling the home office for info, plus we felt it was not for us to tell them what the status is on the case. They need to speak with the employer about that.
>
> Lynn said that Joanne Kader, broker, should have mentioned that to the employer. She will call Joanne and remind her to tell the employer not to refer any calls to the home office. They need to speak with Howard Lowitt [*sic*] or one of the trustees. I also told Lynn that we will not be returning a call to Lance.

Pl. Ex. 10.

Neither of these documents fairly supports a conclusion that Principal was attempting to mislead Burt or any other participant in the Plan. Gowdey's memorandum indicates that Burt called her to find out the balance in his account. At the time of Burt's

inquiry, all of the Plan's assets held by Principal were in a single money market account, because Principal had not received any information from Unitron Graphics allocating the $109,811.28 transfer among the various participants. Gowdey was therefore unable to tell Burt how much money was in his account. Gowdey's memorandum indicates that she communicated this information to Burt. Lee's memorandum essentially confirms these details. Neither document can fairly support a conclusion that Gowdey or Lee was attempting to conceal from Burt the fact that the trustees had not yet accounted for all of the Plan's funds. Plaintiff has therefore failed to demonstrate the existence of a genuine issue of material fact that would preclude summary judgment for Principal as to liability under § 405(a)(1).

B. Liability under § 405(a)(2)

To hold a fiduciary liable under § 405(a)(2), a plaintiff must demonstrate that the fiduciary failed to comply with its duties under ERISA, and thereby enabled a co-fiduciary to commit a breach. For example, as the legislative history to ERISA indicates, a trustee may be liable to a co-trustee in the following circumstances:

> A and B are co-trustees and are to jointly manage the plan's assets. A improperly allows B to have the sole custody of the plan assets and makes no inquiry as to his conduct. B is thereby enabled to sell the property and to embezzle the proceeds. A is to be liable for a breach of fiduciary responsibility.

H.R. Conf. Rep. No. 93-1280, 93d Cong., 2d Sess. 43 (1974), *reprinted in* 1974 U.S.C.C.A.N. 5038, 5080; *see also Restatement (Second) of Trusts* § 224 illus. d (1959) (citing same example). In

this case, the court concludes that plaintiff cannot recover under § 405(a)(2) because Principal's conduct did not enable the trustees to commit a breach. Plaintiff acknowledges that Zucker and Fertig stole the money at issue in this action by drawing checks on a Citibank account over which Principal had no control. By the time Principal acquired any control over the Plan's assets, the money had already been stolen. Plaintiff has not identified any action that Principal could have taken which would have prevented the theft.

Presumably, the real thrust of plaintiff's argument under § 405(a)(2) is that, by failing to take appropriate action when it realized that funds were missing from the Plan, Principal prevented other parties from taking action that might have recovered the funds. Thus argument, however, is relevant to plaintiff's § 405(a)(3) claim, discussed in the next section, rather than § 405(a)(2). For the reasons set forth above, Principal is entitled to summary judgment on plaintiff's claims under § 405(a)(2).

C. Liability under § 405(a)(3)

Plaintiff's strongest argument for holding Principal liable rests on § 405(a)(3). To hold a fiduciary liable under that section, a plaintiff must demonstrate (1) that the fiduciary had knowledge of the co-fiduciary's breach, and (2) that the fiduciary failed to make reasonable efforts under the circumstances to remedy the breach. The court concludes, however, that in order to prevail on a motion for summary judgment, a plaintiff must also be able to identify a reasonable alternative course of action that the fiduciary might have taken that would have prevented a loss to the plan. Because it does not appear that the plaintiff in this case can meet that standard, Principal is entitled to summary judgment on the § 405(a)(3) claim.

Appendix C

The evidence that plaintiff has submitted establishes that, at the latest, Principal became aware that it had not received all of the funds that it expected to receive from Mutual Benefit by November 5, 1991, the date of the first letter to Zucker and Fertig. That letter requested an "immediate" response in the event that the trustees did not intend to forward the funds. The trustees' failure to respond to the November 5 letter was can arguably be viewed as a "red flag" that should have alerted Principal to the possibility that the trustees might be using the Plan's money for an improper purpose. *See Diduck*, 974 F.2d at 283; *Whitney v. Citibank, N.A.*, 782 F.2d 1106, 1116 (2d Cir. 1988). A second red flag was raised when the trustees failed to respond to the second letter on January 28, 1992. At that point, while Principal may not have had any actual evidence of misconduct by the trustees, it had reason to be deeply suspicious.

Principal argues that plaintiff has not produced any evidence demonstrating that it had actual knowledge of any misconduct. In a related context, however, the Second Circuit has held that constructive knowledge of a breach can be sufficient for liability to attach. In *Diduck*, the court held that a non-fiduciary may be liable for knowing participation in a fiduciary's breach of duty. In that context, the court held that the relevant "knowledge" was "knowledge as to the primary violator's status as a fiduciary and knowledge that the primary's conduct contravenes a fiduciary duty." 974 F. 2d at 282-83. With respect to the second prong, it held that "[a] defendant who is on notice that conduct violates a fiduciary duty is chargeable with constructive knowledge of the breach if a reasonably diligent investigation would have revealed the breach." *Id.* at 283. *But see also Lee v. Burkhart*, 991 F.2d 1004, 1011 (2d Cir. 1993) (referring to "actual knowledge" as component of possible claim under § 405(a)(3)). The court therefore will assume, for the purposes of this opinion, that the

evidence in the record creates a genuine issue of fact as to whether Principal had sufficient knowledge of the breach to trigger its duty under § 405(a)(3) to make reasonable efforts to remedy the breach.

The evidence that plaintiff has submitted also raises genuine issues of fact as to whether Principal's conduct was reasonable under the circumstances, given what it knew about the missing funds. Assuming that Principal was justified in waiting until November 5, 1991, to contact the trustees about the missing funds, the record contains no explanation of Principal's subsequent inaction. In spite of the letter's stern warning that the missing funds "must be accounted for" and its request that the trustees immediately notify Principal if they did not intend to forward the funds, Principal took no action until January 28, 1992 — a full twelve weeks later. Having sent an even more emphatic warning in its follow-up letter, Principal then did nothing for another eight weeks, until the Department of Labor initiated its investigation. Although plaintiff overstates his case when he claims Principal did nothing, this response can hardly be characterized as swift. Given the warning signs it had received, Principal would have been wise to act at a less glacial pace.

The court concludes, however, that to prevail in this action, plaintiff must do more than show that Principal failed to make reasonable efforts to remedy the trustees breach. He must also show that, if Principal had made such efforts, the loss to the Plan, or at least some portion of it, could have been prevented. To be sure, § 405(a)(3) does not, on its face, contain any such requirement of causation. As written, the statute appears to impose liability on a fiduciary *whenever* it has knowledge of a breach, and fails to make reasonable efforts under the circumstances to remedy the breach.

Nor are the authorities that Principal cites in support of its claim that § 405(a)(3) contains a causation requirement highly persuasive. Neither the district court opinion nor the Seventh Circuit's opinion in *Brandt* addressed § 405(a)(3) at all. Those opinions merely held that the language of § 405(a)(2) implies a causal link between a fiduciary's misconduct and loss to a plan. *Omni Funding Group* concluded that § 405(a)(3) requires a causal link, but did not identify a clear textual basis for that conclusion, concluding simply that it was necessary to prevent "manifest unfairness." 731 F. Supp. at 176. In *Brink v. DaLesio*, 496 F. Supp. 1350 (1980), *aff'd in part and rev'd on other grounds*, 667 F.2d 420 (4th Cir. 1981), the court held that § 405(a) requires a causal link. The opinion, however, simply restates the language of § 405(a) and cites to its legislative history, without specifically discussing § 405(a)(3).[5]

Nonetheless, the court is persuaded that plaintiff cannot prevail in this action without showing that, but for Principal's actions, all or part of the loss to the Plan could have been prevented. As discussed above, the jurisdictional vehicle for this lawsuit is § 502(a)(2) of ERISA, which allows fiduciaries to sue for appropriate relief under § 409. It is beyond dispute that § 409 requires a showing of causation. *See Diduck*, 974 F.2d at 270; *Brandt*, 687 F.2d at 898. The plain language of that statute makes a fiduciary liable for "losses to the plan *resulting* from . . . [a] breach." 29 U.S.C. § 1109 (emphasis added). In this respect, as

---

5. Many of the cases on which Principal relies do not involve co-fiduciary liability under § 405(a) at all. They simply hold that a fiduciary may not be liable as a primary violator unless his actions cause a loss. *E.g. Whitfield v. Lindemann*, 853 F.2d 1298, 1304 (5th Cir. 1988), *cert. denied*, 490 U.S. 1089 (1989); *Hecht v. Colorboard Packaging Corp.*, 856 F. Supp. 184, 190 (S.D.N.Y. 1994); *Kuper v. Quantum Chemicals Corp.*, 852 F. Supp. 1389, 1396 (S.D. Ohio 1994), *aff'd*, 66 F.3d 1447 (6th Cir. 1995).

in many others, ERISA is similar to the common law of trusts, under which a trustee is liable for a breach of trust only to the extent that the breach causes loss. *See Restatement (Second) of Trusts* § 205 (1959). Since this action must arise under § 502(a)(2), for reasons discussed above, plaintiff is bound by the requirements of § 409 as well as § 405. Plaintiff therefore can recover against Principal only to the extent that its actions actually caused a loss to the Plan.

Plaintiff also suggests that, once he has shown a breach, the burden of persuasion should shift to Principal to demonstrate a lack of causation. That argument stems from a misreading of *Martin v. Feilen*, 965 F.2d 660, 671 (8th Cir. 1992), *cert. denied*, 506 U.S. 1054 (1993). The issue in *Martin* involved the calculation of damages after a plaintiff has proved a prima facia case of loss to the plan or resulting from a breach of duty. Once a prima facie case of causation has been proved, the burden shifts to the defendant to demonstrate that any loss to the plan, or profit to the fiduciary, did not result from the breach. *See Donovan v. Bierwirth*, 754 F.2d 1049, 1056 (2d Cir. 1985). The initial burden of proving causation, however, rests with the plaintiff.

To prevail, then, plaintiff must demonstrate not only that Principal failed to take reasonable steps to remedy the breach. He must be able to show that, if Principal had taken reasonable steps, at least some portion of the loss to the Plan could have been prevented. If reasonable efforts could not have remedied the breach, Principal cannot be held liable. Moreover, in order to survive a motion for summary judgment, plaintiff must "do more than simply show that there is some metaphysical doubt as to the material facts," *Heilweil v. Mount Sinai Hosp.*, 32 F.3d 718, 723 (2d Cir. 1994) (citations and internal quotations omitted), *cert. denied*, 115 S. Ct. 1095 (1995). He must "produce 'significant

probative evidence tending to support [his position].' " *Project Release v. Prevost*, 722 F.2d 960, 968 (2d Cir. 1983) (quoting *United States v. Pent-R-Books, Inc.*, 538 F.2d 519, 529 (2d Cir. 1976), *cert. denied*, 430 U.S. 906 (1977)). At the very least, then, plaintiff must demonstrate that some reasonable alternative course of conduct would have prevented the loss.

Plaintiff has not met this burden. Although he repeatedly claims that Principal took no action at all to recover the missing funds, nowhere does he state what Principal might have done, or explain how such action could have led to the recovery of the money. As the legislative history to ERISA notes, the question of what efforts a fiduciary must take to remedy a co-fiduciary's breach is highly fact-specific, depending on "the relationship of the fiduciary to the plan and to the co-fiduciary, the duties and responsibilities of the fiduciary in question, and the nature of the breach." H.R. Conf. Rep. 93-406, 1974 U.S.C.C.A.N. at 5080. Depending on the circumstances, the appropriate remedy may be "to notify the plan sponsor of the breach or to proceed to an appropriate Federal court for instructions, or to bring the matter to the attention of the Secretary of Labor." *Id*; *see also Morrissey v. Curran*, 567 F.2d 546, 550 (2d Cir. 1977) (Lumbard, J. concurring) (quoting above language from House conference report). To demonstrate that any of these actions could have resulted in a recovery to the Plan, plaintiff would have to produce some evidence concerning what the trustees did with the money and what their financial condition was during the relevant time period.

Plaintiff has not produced sufficient evidence concerning these matters to raise a genuine issue of material fact. Indeed, he acknowledged in response to interrogatories posed by Principal that he had not investigated what the trustees did with the money

because he considered it irrelevant to this action. Wolfson Aff., Ex. F. The only evidence that plaintiff has submitted concerning the financial condition of the trustees and of Unitron Graphics consists of a portion of a bankruptcy petition filed by Unitron Graphics pursuant to Chapter 11 of the Bankruptcy Code and a confidential internal memorandum, written on Unitron Graphics stationary, describing a tentative plan of reorganization. The petition appears to have been filed on January 6, 1992, and the memorandum is dated September 7, 1992. These documents do indicate that Unitron Graphics had assets in excess of its liabilities to secured creditors. In response, however, Principal has submitted copies of two orders of the Bankruptcy Court. Those orders indicate that Unitron Graphics never submitted a reorganization plan and that the case was converted into a proceeding under Chapter 7 of the Bankruptcy Code. Furthermore, Principal has submitted a copy of the bankruptcy trustee's report, dated July 23, 1993, stating that he had not "received any property nor paid any money on account of this estate except exempt property" and that, after conducting a diligent inquiry into the debtor's affairs, he had determined that "there is no property available for distribution from the estate over and above that exempted by law. . . ." Wolfson Rep. Aff. Ex. C. Thus it appears that Unitron Graphics did not have sufficient assets to pay any of its unsecured creditors. In light of this subsequent determination, plaintiff's submissions do not raise any genuine issue of material fact as to whether Principal could have recovered the missing funds from Unitron Graphics.[6]

---

6. Plaintiff also claims that the bankruptcy petition indicates that Zucker and Fertig were continuing to receive a combined $6,700 per week during the period that Unitron Graphics was in the Chapter 11 proceeding. That statement is somewhat misleading. In an affidavit filed pursuant to Local Bankruptcy Rule 11, Fertig stated that that amount was "now being paid and proposed to be paid

(Cont'd)

Plaintiff also argues that the fact that Zucker and Fertig have been able to make partial restitution to the Plan in the wake of their criminal prosecution suggests that Principal could have recovered even more money from them if it had acted sooner. This conclusion is unsupported by the record. Plaintiff has submitted no evidence as to the financial condition of the trustees in the relevant period, and documents submitted by Principal indicate that the restitution payments Zucker and Fertig did make came from money that they borrowed, rather than from their personal assets.

Without some indication from plaintiff as to what Principal might have done to remedy the trustees' breach, given the specific knowledge that it possessed, and some explanation of how such action would have benefitted the Plan, the court cannot conclude that Principal's conduct caused a loss. Since proof of causation is an essential element of plaintiff's action, Principal is entitled to summary judgment.

CONCLUSION

For the foregoing reasons, Principal's motion for summary judgment is granted, and plaintiffs motion is denied. Furthermore, since plaintiff does not seek any relief against Zucker and Fertig, the sole remaining defendants, this action is dismissed without prejudice against them. In addition, all cross-claims and counter-claims are dismissed as moot. The Clerk of the Court is instructed to enter judgment accordingly.

(Cont'd)

. . . for a period of thirty days following the filing of the Chapter 11 petition." Plaintiff has submitted no evidence that this money was actually paid subsequent to the filing of the petition. Furthermore, without some additional evidence as to the trustees' overall financial condition, the fact that they drew a salary in the period prior to filing the petition does not indicate that they would have been able to restore any of the money they had stolen.

Appendix C

s/ Allyne R. Ross
Allyne R. Ross
United States District Judge

Dated: May 16, 1996
Brooklyn, New York

APPENDIX D — JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF NEW YORK FILED MAY 29, 1996

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

95-CV-0500 (ARR)

DAVID W. SILVERMAN,

Plaintiff,

-against-

MUTUAL BENEFIT LIFE INSURANCE CO., et al.,

Defendants.

JUDGMENT

An opinion and order of Honorable Allyne R. Ross, United States District Judge, having been filed on May 21, 1996, granting defendant Mutual Benefit Life Insurance Co.'s motion for summary judgment; denying plaintiff's cross-motion for summary judgment; dismissing the action without prejudice against the sole remaining defendants, Zucker and Fertig; and dismissing all cross-claims and counter-claims as moot, it is

ORDERED AND ADJUDGED that plaintiff take nothing of the defendants; that defendant Mutual Benefit Life Insurance Co.'s motion for summary judgment is granted; that plaintiff's cross-motion for summary judgment is denied; that the action is dismissed without prejudice against the sole remaining defendants, Zucker and Fertig; and, that all cross-claims and counter-claims are dismissed as moot.

Appendix D

Dated: Brooklyn, New York
May 28, 1996

s/ Robert C. Heinemann
ROBERT C. HEINEMANN
Clerk of Court

APPENDIX E — AMENDED JUDGMENT OF THE UNITED STATES COURT OF APPEALS FOR THE EASTERN DISTRICT OF NEW YORK FILED JUNE 17, 1996

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

95-CV-0500 (ARR)

DAVID W. SILVERMAN,

Plaintiff,

-against-

MUTUAL BENEFIT LIFE INSURANCE CO., et al.,

Defendants.

AMENDED JUDGMENT

A memorandum and order of Honorable Allyne R. Ross, United States District Judge, having been filed on May 21, 1996, granting defendant Principal Mutual Life Insurance Co.'s motion for summary judgment; denying plaintiff's cross-motion for summary judgment; dismissing the action without prejudice against the sole remaining defendants, Zucker and Fertig; dismissing all cross-claims and counter-claims as moot; and, a separate opinion and order having been filed on April 22, 1996, granting defendant Mutual Benefit Life Insurance Co.'s motion for summary judgment, it is

ORDERED AND ADJUDGED that plaintiff take nothing of the defendants; that defendants' motions for summary judgment

are granted; that plaintiff's cross-motion for summary judgment is denied; that the action is dismissed without prejudice against the sole remaining defendants, Zucker and Fertig; and, that all cross-claims and counter-claims are dismissed as moot.

Dated: Brooklyn, New York
June 12, 1996

s/ Robert C. Heinemann
ROBERT C. HEINEMANN
Clerk of Court

APPENDIX F — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT DENYING PETITION FOR REHEARING FILED APRIL 27, 1998

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
UNITED STATES COURT HOUSE
40 FOLEY SQUARE
NEW YORK 10007

GEORGE LANGE III
CLERK

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, Foley Square, in the City of New York, on the 27th day of April one thousand nine hundred and ninety-eight.

Dkt No.: 96-7795

Silverman

v

Mutual Benefit et al

A petition for rehearing containing a suggestion that the action be *reheard* in banc having been filed herein by the appellant David W. Silverman, as Independent Fiduciary of the Unitron Graphics, Inc., Profit Sharing Trust and Unitron Graphics, Inc. Profit Sharing Trust-Union and Non-Union Division,

Upon consideration by the panel that decided the appeal, it is Ordered that said petition for rehearing is **DENIED.**

Appendix F

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges for the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

FOR THE COURT

GEORGE LANGE III, Clerk

By: s/ Beth J. Meador
Beth J. Meador,
Administrative Attorney

Supreme Court, U.S.
FILED
AUG 24 1998
OFFICE OF THE CLERK

No. 98-174

In The

Supreme Court of the United States

October Term, 1997

DAVID W. SILVERMAN, as Independent Fiduciary of The Unitron Graphics, Inc. Profit Sharing Trust and Unitron Graphics, Inc. Profit Sharing Trust-Union and Non-Union Division,

Petitioner,

vs.

MUTUAL BENEFIT LIFE INSURANCE COMPANY, PRINCIPAL MUTUAL LIFE INSURANCE COMPANY and HELENE GORNY,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF IN OPPOSITION FOR RESPONDENTS MUTUAL BENEFIT LIFE INSURANCE COMPANY AND HELENE GORNY

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COUNSEL PRESS

QUESTION PRESENTED

1. Did the Second Circuit err in concluding that Respondents Mutual Benefit Life Insurance Company ("Mutual Benefit"), and one of its employees, Helene Gorny ("Gorny"), had not breached their ERISA fiduciary duties in complying with a facially valid notice from a trustee of an employee profit sharing plan discontinuing the investment contract and directing the transfer of funds to the trustees.

PARTIES TO THE PROCEEDING

The petition accurately lists the parties to the proceeding.

There or no publicly-owned parent or subsidiary company of respondent Mutual Benefit Life Insurance Company.

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29 U.S.C. § 1104(c) 9

STATEMENT OF THE CASE

A. Nature of Case and Course of Proceedings

This petition seeks this Court's review of the Second Circuit's well-reasoned opinion affirming the District Court's grant of summary judgment to Mutual Benefit and Gorny and to Principal Mutual Life Insurance Company ("Principal") (Pet. pp. 1a-20a).[1] Petitioner thereafter sought rehearing and *en banc* consideration. The Second Circuit denied the motion in all respects. (Pet. pp. 72a-73a). Petitioner now seeks a Writ of Certiorari from this Court.

Following the issuance of the District Court's decisions, the United States Department of Labor obtained leave to file an amicus brief in support of the appeal against Principal. The Department of Labor apparently found nothing objectionable with the District Court's holding concerning Mutual Benefit and Gorny and its *amicus* brief to the Second Circuit did not address any issues regarding them.

B. Statement of Facts

The decisions below turned on their own peculiar facts and, as such, will not affect anyone other than the litigants. The unique and undisputed facts were set forth in the Second Circuit decision:

> In 1988, Unitron Graphics, Inc. ("Unitron") established the plan [the Unitron Graphics, Inc. Profit Sharing Trust and the Unitron Graphics, Inc.

1. Principal succeeded Mutual Benefit as the investment manager of certain of Petitioner's profit sharing plan investments. This brief is submitted only behalf of Mutual Benefit and Gorny and is addressed to the arguments made at pages 5-10, 15-21 of the Petition.

Profit Sharing Trust-Union and Non-Union Division (the "Plan")] for employee profit-sharing.[2] It was established as an "individual account" or "defined contribution" ERISA plan under 29 U.S.C. § 1002 (34). Each participating employee could elect to have Unitron set aside part of his salary as a contribution to the plan; in addition, [Unitron] could make matching and discretionary contributions.

The plan had two named trustees: Jacob Zucker and Aaron Fertig, who are owners and officers of Unitron. The plan provided that joint trustees "shall act by a majority of their number but may authorize one or more of them to sign all papers on their behalf." It further provided that Mutual Benefit "may rely on the signature of any Trustee on . . . any document used in connection with" a plan-related contract.

The plan's assets were invested pursuant to a group annuity contract between the Trustees and Mutual Benefit. The Trustees retained the right to cancel the contract at any time.

Mutual Benefit experienced well-publicized financial problems in the Spring and Summer of 1991, which culminated in a July 16th, 1991 order of the Superior Court of New Jersey placing Mutual Benefit into court-supervised rehabilitation.

On July 1, 1991, Zucker wrote to Mutual Benefit to cancel the contract. The letter was on Unitron

2. Mutual Benefit and Gorny were not signatories to the 401(k) Plan, nor were either identified as a Trustee, Plan Administrator or a "named fiduciary" in the Plan (*see* App. p. 149 defining "Trustee" and "Plan Administrator" and App. p. 164 naming "Fiduciaries").

stationary and was signed by Zucker as trustee. The letter requested that Mutual Benefit return the plan funds to Unitron, along with an accounting breakdown for each plan participant. Mutual Benefit did not send the funds to Unitron, apparently because the funds could not properly be paid to the company but only to the trustees in their fiduciary capacity.

On August 15, 1991, Zucker, as plan trustee, wrote a second letter to Mutual Benefit. This letter instructed that the assets of the plan be remitted to the Unitron Graphics, Inc. profit sharing trust with a breakdown by participant.

Accordingly, Mutual Benefit liquidated the fund's investments and defendant Gorny, a Mutual Benefit customer service supervisor, approved a check requisition.[3] On August 30, 1991, Mutual Benefit sent Zucker a check for the proceeds in the amount of $239,811.28 payable to the plan.

Zucker deposited the check in the plan's bank account on September 6, 1991. Over the next few weeks, Zucker and Fertig embezzled $130,000 from the account.[4]

(Pet. pp. 4a-6a).

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3. Gorny's written approval of the check requisition, which requisition had been prepared by a Mutual Benefit service representative, constituted the extent of Gorny's involvement in the events that underlie this action. (App. 233, 235-36).

4. Zucker and Fertig pled guilty to embezzlement including monies belonging to the 401(k) Plan. Judge Glasser sentenced them and also removed them as Trustees of the 401(k) Plan and appointed Petitioner as the independent fiduciary of the Plan, succeeding to Zucker's and Fertig's role (App. 85-89).

REASONS FOR DENYING THE WRIT

I.

THE COURTS BELOW CORRECTLY FOUND THAT MUTUAL BENEFIT AND GORNY DID NOT BREACH THEIR FIDUCIARY DUTIES OR CONTRACTUAL DUTIES IN COMPLYING WITH A WRITTEN DIRECTION FROM A TRUSTEE OF THE 401(k) PLAN TO DISCONTINUE THE INVESTMENT CONTRACT AND TRANSMIT THE FUNDS TO THE 401(k) PLAN.

Petitioner reasserts the same arguments to this Court as he made to the underlying federal courts, namely that Mutual Benefit and Gorny breached their fiduciary duties by not inquiring "as to why a single trustee [Zucker] . . . had issued a direction to transfer certain pension accounts." (Pet. p. 20). The courts below conducted extensive analyses of the record and determined that no breach had occurred. Those decisions are correct applications of the settled law, based on unique circumstances that are not likely to present themselves again, and, consequently, do not warrant review by this Court.

The District Court expressly held that

> [u]nder the terms of the Contract . . . , once the trustees [Zucker and Fertig] made a request for the release of the Plan's funds, Mutual Benefit [and Gorny] had no authority to refuse it.

(Pet. 30a). The District Court also rejected petitioner's argument that:

> [B]ecause the [July 1, 1991 and August 15, 1991] letters were signed by only one trustee, Zucker,

Mutual Benefit and Gorny should have suspected that something was amiss, [noting]:

> Even leaving aside the fact that the co-trustee, Fertig, was also involved in the subsequent embezzlement, this argument is unpersuasive. As Mutual Benefit and Gorny note, the written agreement establishing the Plan specifically provided that "[t]he Insurer [Mutual Benefit] may rely on the signature of any Trustee on an application for or any document used in connection with a Contract or Policy." (Pet. p. 32a quoting App. p. 165), [and that,] [a]s fiduciaries, Mutual Benefit and Gorny were required to discharge their duties in accordance with the written terms of the Plan. 29 U.S.C. § 1104(a)(1)(d).

Pet. p. 32a.[5]

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5. The District Court also stressed that the Contract between the trustees and Mutual Benefit provided that:

> We [Mutual Benefit] are entitled to assume that the Plan permits any action taken by you [the trustees]. We are not a party to the Plan, and are not responsible for its validity. Except as expressly provided in this contract or any other written agreement accepting responsibility, we are not responsible for any duties under the Plan or for any duties of the Plan administrator or named fiduciary.
>
> We may rely on any action taken by you under this contract, and will be held harmless and completely discharged when acting on your direction or authorization.

App. p. 126, "Exoneration".

Similarly, the Second Circuit ruled that:

> Mutual Benefit's transfer of Plan funds to Zucker, in the form of a check made out to the Plan, complied fully with the terms of Mutual Benefit's contract with the plan . . . Upon written notice of discontinuance, Mutual Benefit was required to return to the Plan all "Investment Accounts held under this contract."
>
> The transfer of plan funds also complied fully with the terms of the plan itself. . . . Under the terms of the plan, the joint trustees "may authorize one or more of them to sign all papers on their behalf." The plan further provided that Mutual Benefit "may rely on the signature of any Trustee on any application for or any document used in connection with" its contract with the plan. The plan delegated to Zucker the authority to act on behalf of both trustees in documents used in connection with the plan, and Mutual Benefit lawfully relied on this authority in connection with cancellation of the contract.
>
> * * *
>
> Mutual Benefit had no duty of inquiry pursuant to § 1104(a)(1)(B) prior to releasing plan funds to Zucker. It had no reason to be suspicious of Zucker's cancellation of the contract . . . Mutual Benefit's financial problem in the Spring and Summer of 1991 provided ample reason for the cancellation. Zucker's cancellation request complied fully with the terms of all relevant plan documents and the contract itself . . . Summary

judgment was properly granted in favor of Mutual Benefit and Gorny.

Pet. pp. 10a-11a.

As held, Mutual Benefit was contractually bound to respond to the written direction of the Trustee and its conduct in doing so was, in all respects, proper. Moreover, Mutual Benefit is not clairvoyant and had no means to discern the intentions of Zucker an Fertig to embezzle the funds, if indeed that was their intention in July-August, 1991. Indeed, petitioner's argument is totally unworkable as it would require every fiduciary to inquire as to the trustee's motive before obeying any basically valid contractual directive. No financial institution would serve under such a rule.

Petitioner cites a few cases for general propositions that have no bearing on the case at bar. *Matthews v. Sears Pension Plan*, 144 F.3d 1041 (7th Cir. 1998), for example, is cited for the Court's discussion of contract interpretation in ERISA matters. Petitioner here does not identify any particular contractual term that petitioner contends was misinterpreted.

Petitioner also cites a series of cases for the general proposition that "[a] fiduciary's obligation to a participant is only extinguished when adequate provisions have been made for the continued prudent management of plan assets." Pet. p. 19.[6] Here, whatever fiduciary duty Mutual Benefit and Gorny had with respect to the Plan funds was extinguished when the funds were transferred at the written request of the Trustees

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6. *Chambers v. Kaleidoscope, Inc. Profit Sharing Plan*, 650 F. Supp. 359, 369 (N.D. 1986); *Pensions Benefit Guaranty Corp. v. Greene*, 520 F. Supp. 1483 (W.D. Pa. 1983), *aff'd mem.*, 727 F.2d 1100 (3d Cir.) *cert. den.*, 469 U.S. 820, 105 S. Ct. 92, 83 L. Ed. 2d 38 (1984); and *Freund v. Marshall & Isley Bank*, 485 F. Supp. 629 (W.D. Wis. 1979).

and deposited in the Plan's bank account. The actual loss sustained by the 401(k) Plan was not caused by the transferring of the funds to the Plan's bank account; the loss resulted weeks thereafter from the superseding criminal conduct of Zucker and Fertig in embezzling $130,000 of those monies.[7]

Petitioner's reliance on *Firstier Bank, N.A. v. Zeller*, 16 F.3d 907, 910-11 (8th Cir. 1994) is misplaced since there, under strikingly similar circumstances, the Eighth Circuit held that

> [b]ecause Firstier obeyed the Plan and the statute, the participants may not shift to Firstier responsibility for their own subsequent loss of the proceeds or for the unknown misdeeds of another fiduciary, Dombroski. Thus, on the specific facts of this case . . . Firstier had no duty to inquire.

16 F.3d at 913.

II.

THE SECOND CIRCUIT IMPLICITLY REJECTED PETITIONER'S ARGUMENT THAT MUTUAL BENEFIT AND GORNY HAD AN OBLIGATION TO OBTAIN THE APPROVAL OF THE PLAN PARTICIPANTS BEFORE COMPLYING WITH THE WRITTEN DIRECTION OF A TRUSTEE.

Petitioner erroneously argues that the Second Circuit "ignored" his argument that Mutual Benefit "allowed an unauthorized party [the Trustees, Zucker and Fertig] to make

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7. *See Whitfield v. Lindemann*, 853 F.2d 1298, 1304 (5th Cir. 1988), *cert. denied sub nom, Klepak v. Dole*, 490 U.S. 1089, 109 S. Ct. 2428 (1989); *Brandt v. Grounds*, 502 F. Supp. 598 (N.D. Ill, 1980), *aff'd*, 697 F.2d 895, 897 (7th Cir. 1982).

an investment decision *i.e.*, liquidate certain investment accounts and transfer the amount," claiming that the participants alone could make such so-called investment decisions. (Pet. p. 16). The Second Circuit did not "ignore" the argument, it impliedly rejected it or, alternatively, refused to consider it because petitioner had not raised it in the District Court (Pet. p. 12a). In any event, the argument is specious since the statutes on which petitioner relies, 29 U.S.C. § 1104(c) and 26 U.S.C. § 401(k)(10)(A)(i), simply provide that ERISA fiduciaries, in discharging their duties in the interests of participants and beneficiaries, must invest prudently and in accordance with the documents and instruments governing the plan. Nowhere do they provide that investment management decision-making rests with the participants.

It was the Trustees here, not the participants, who were authorized by the Plan documents to determine with whom to invest the 401(k) Plan contributions and the Trustees here chose to invest them in a funding vehicle provided by Mutual Benefit.[8] The participants were not empowered to invest their contributions in investment vehicles other than those offered by Mutual Benefit's or to terminate the Contract and invest all of the 401(k) Plan contributions elsewhere. The authority for making those decisions rested solely with the Trustees.[9]

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8. The participants' exercise of control was limited to "choos[ing] among the various Investment Accounts defined in the Contract . . . change their choices and transfer between Investment Accounts, as permitted in the Contract." (*See* App. p. 152, Article VI, "Investment of Contributions", para. 2). Plan participants (Unitron employees) could, for example, choose to invest their contributions in any one of four "separate" accounts (Equity Growth, Aggressive Equity, Short Term Money Market and Real Estate) in which the rate of return fluctuated according to a variety of economic and financial events affecting the accounts' investments. *See* App. pp. 109-17 for a description of the accounts.

9. The trustees of the 401(k) Plan were charged with the (Cont'd)

Nothing in the Plan documents compelled the Trustees to seek the permission of the participants prior to terminating the Contract. As for Mutual Benefit and Gorny, they had no input into the decision of the Trustees and had no contractual or statutory obligation to report the decision to the participants.

III.

NO GENUINE CONFLICT OF AUTHORITY EXISTS REGARDING THE DUTY OF INQUIRY ON THE PART OF MUTUAL BENEFIT AND GORNY.

Petitioner does not allege that there exists a conflict between the circuits on the law regarding the alleged duty of inquiry on the part of Mutual Benefit and Gorny, or regarding any other aspect of his claim against these Respondents. Moreover, petitioner does not allege, let alone demonstrate that any other Circuit would have held differently had it been presented with the unique facts at issue here. Indeed, the Eighth Circuit in *Firstier Bank N.A. v. Zeller*, 16 F.3d at 910-11, held, on analogous facts, precisely as the Second Circuit did here.

(Cont'd)
responsibility of choosing the appropriate investment vehicle for the participants funds. If they could not discontinue the Contract and move the funds elsewhere according to their best judgment, they could not effectively discharge this responsibility. Thus, if participants could individually elect to discontinue or not discontinue the Contract as to his or her accounts and enter into other contracts with different investment managers, the Plan would be unworkable.

CONCLUSION

For all the reasons set forth above, Respondents respectfully request that this court deny the Petition for Writ of Certiorari.

Respectfully submitted,

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No. 98-174

In The

Supreme Court of the United States

October Term, 1997

DAVID W. SILVERMAN, as Independent Fiduciary of The Unitron Graphics, Inc. Profit Sharing Trust and Unitron Graphics, Inc. Profit Sharing Trust-Union and Non-Union Division,

Petitioner,

vs.

MUTUAL BENEFIT LIFE INSURANCE COMPANY, PRINCIPAL MUTUAL LIFE INSURANCE COMPANY and HELENE GORNY,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF IN OPPOSITION FOR RESPONDENT PRINCIPAL MUTUAL LIFE INSURANCE COMPANY

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COUNTERSTATEMENT OF QUESTION PRESENTED[1]

Whether the Second Circuit Court of Appeals properly affirmed the district court's dismissal of Petitioner's claim against Principal for breach of co-fiduciary obligations under § 405(a) of the Employee Retirement Income Security Act of 1974, as amended, 29 U.S.C. § 1105(a) (1994) ("ERISA").

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1. This brief in opposition addresses only those portions of Petitioner, David W. Silverman, as Independent Fiduciary of The Unitron Graphics, Inc. Profit Sharing Trust and Unitron Graphics, Inc. Profit Sharing Trust-Union and Non-Union Division ("Petitioner" or "Silverman")'s Petition for Writ of Certiorari that relate to Respondent Principal Mutual Life Insurance Company ("Principal").

PARTIES TO THE PROCEEDING

The petition correctly names the parties to the proceeding, but incorrectly states that Principal, Mutual Benefit Life Insurance Company ("Mutual Benefit"), and Helene Gorny ("Gorny") were defendants-appellants. Defendants were appellees in the Second Circuit Court of Appeals.

STATEMENT PURSUANT TO RULE 29.6

Principal Mutual Life Insurance Company ("Principal") states that it was reorganized effective July 1, 1998. Principal Mutual Holding Company now wholly owns Principal Life Insurance Company. Principal Life Insurance Company has no corporate parents or nonwholly owned subsidiaries that have issued shares to the public other than:

United Payors & United Providers, Inc.
Sloans Lake Management Corp.

Principal has also organized the following Mutual Funds:

Principal Aggressive Growth Fund, Inc.
Principal Asset Allocation Fund, Inc.
Princor Balanced Fund, Inc.
Principal Balanced Fund, Inc.
Princor Blue Chip Fund, Inc.
Princor Bond Fund, Inc.
Principal Bond Fund, Inc.
Princor Capital Accumulation Fund, Inc.
Principal Capital Accumulation Fund, Inc.
Princor Cash Management Fund, Inc.
Principal Money Market Fund, Inc.
Princor Emerging Growth Fund, Inc.
Principal Emerging Growth Fund, Inc.

Princor Government Securities Income Fund, Inc.
Principal Government Securities Fund, Inc.
Princor Growth Fund, Inc.
Principal Growth Fund, Inc.
Princor High Yield Fund, Inc.
Principal High Yield Fund, Inc.
Princor Tax-Exempt Bond Fund, Inc.
Princor Tax-Exempt Cash Management Fund, Inc.
Princor Utilities Fund, Inc.
Princor World Fund, Inc.
Principal World Fund, Inc.
Principal Special Markets Fund, Inc.

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APPENDIX

Appendix A — Relevant Statutes Involved 1a

PERTINENT STATUTORY PROVISIONS

The statutory provisions involved with respect to Petitioner's claim against Principal are 29 U.S.C. § 1105(a) (1994), 29 U.S.C. § 1109 (1994) and 29 U.S.C. § 1132(a) (1994 & Supp. II 1996). These statutes have been set forth in full in the Appendix hereto.

COUNTERSTATEMENT OF THE CASE

On August 30, 1991, Mutual Benefit, the first investment manager of the Unitron Graphics, Inc. Profit Sharing Trust-Union and Non-Union Divisions (the "401(k) plans"), released $239,811.28 of the 401(k) plans' assets to Jacob Zucker and Aaron Fertig, the plans' named trustees and fiduciaries (A-5a-6a).[2] Immediately upon their receipt in September 1991 of the 401(k) plans' assets, Zucker and Fertig embezzled $130,000 (A-6a). The funds were embezzled before Principal, who was to take over administration and investment of the 401(k) plans, received the remaining $109,811.28 from Unitron Graphics (A-6a). Although Principal sent letters to Zucker and Fertig demanding that the remaining $130,000 released by Mutual Benefit be accounted for, its efforts were to no avail. Within six months, Unitron Graphics had filed for bankruptcy and the United States Department of Labor was investigating Zucker's and Fertig's actions (A-7a-8a). Eventually, Zucker and Fertig were indicted and pled guilty. As part of their sentence, they were ordered to pay restitution to the 401(k) plans (A-8a). However, "Zucker and Fertig proved to be insolvent" (A-8a).

Petitioner, who was appointed by the court in the criminal action to effectuate payment of restitution, commenced this action against Mutual Benefit, its employee Gorny and

2. References to the Appendix to the Petition for Writ of Certiorari are cited as A-__ .

Principal. Petitioner charged that Mutual Benefit and Gorny breached their fiduciary duties by improperly transferring $239,811.28 of the 401(k) plans' assets to Zucker and Fertig and that Principal breached its co-fiduciary obligations by allegedly failing to take appropriate action when it received, on October 8, 1991, only $109,811.28 of the $239,811.28 released by Mutual Benefit (A-9a). The district court granted summary judgment to Principal and the Second Circuit affirmed.

With respect to Principal, the issue on this Petition for Writ of Certiorari is whether this Court should review the Second Circuit Court of Appeals' ruling that, to recover damages for breach of co-fiduciary obligations under 29 U.S.C. § 1105(a), Petitioner had the burden of proving that Principal's alleged breach resulted in a loss to the 401(k) plans. Review is not warranted for a number of reasons. Contrary to Petitioner's assertion, the Second Circuit's decision does not subvert the goals of ERISA by granting investment managers unwarranted broad protection from liability for their improper conduct (Petition for Writ of Certiorari ("Pet.") at 4). The Second Circuit did nothing more than apply the plain language of sections 405(a) and 409(a) of ERISA and well-settled case law in determining that, where compensatory damages are sought, the plaintiff bears the burden of proving that the plan's losses resulted from the defendant's breach of co-fiduciary obligations.

There is no conflict between the Second Circuit and other circuits on this point. To the contrary, courts have uniformly held that, to recover monetary damages, a plaintiff must prove that a breach of fiduciary or co-fiduciary duty resulted in a loss to the ERISA plan. The authorities relied upon by Petitioner merely stand for the unremarkable proposition that once the plaintiff has met its burden of showing that the breach of

fiduciary duty at issue resulted in a plan loss, the burden of contradicting that showing or presenting another defense shifts to the defendant.

The Second Circuit found that Petitioner did not meet his threshold burden of demonstrating a causal connection between Principal's alleged breach of co-fiduciary obligations and the 401(k) plans' loss. Since Petitioner declined to show *any* connection between the alleged breach and the loss, the Second Circuit never even reached the issue of shifting the burden to Principal to disprove damages or otherwise present another defense. Indeed, in the courts below, Petitioner repeatedly argued for imposition of strict liability and that causation was not an element of a claim for breach of co-fiduciary obligations. Petitioner's current attempt to urge this Court to adopt a standard that would excuse a plaintiff from coming forward with any evidence on one of the elements of its claim — a causal connection between the defendant's conduct and the loss to the plan — conflicts with the plain language of the statute, finds no basis in the case law and should be rejected.

Further, this action presents a unique factual situation that does not warrant review. To the extent that any authorities can be construed to place the burden on a fiduciary to disprove causation, those cases involved direct actions against the fiduciaries who engaged in self-dealing, prohibited transactions or active misconduct, which rendered it impossible to calculate damages after liability was established. There are no such facts in this case. To excuse Petitioner from establishing an element of his *prima facie* case under the facts presented here not only finds no support in the law, but it would also greatly expand the burdens placed on investment advisers, essentially rendering them insurers for conduct of the named trustees and fiduciaries of a plan.

A. The 401(k) Plans' Contract with Mutual Benefit and Mutual Benefit's Transfer of $239,811.28 in Plan Assets to Zucker and Fertig

The 401(k) plans were established by Unitron Graphics in July 1988, pursuant to section 401(k) of the Internal Revenue Code, for the purpose of providing retirement benefits to both the union and non-union employees of Unitron Graphics. Jacob Zucker and Aaron Fertig were the named fiduciaries and trustees of those plans as well as officers of Unitron Graphics (A-4a-5a). When the plans were first established, "[t]he plan's assets were invested pursuant to a group annuity contract between the trustees and Mutual Benefit" (A-5a). However, in mid-1991, when Mutual Benefit was experiencing well publicized financial problems, the trustees terminated the 401(k) plans' relationship with Mutual Benefit and, in early July 1991, contracted with Principal to act as investment manager (A-5a-6a).

On August 30, 1991, Mutual Benefit issued to Zucker a check in the amount of $239,811.28 payable to the 401(k) plans (A-6a). Principal had no contact with Mutual Benefit regarding the transfer of the 401(k) plan monies held by it (JA-431, ¶ 10).[3] Accordingly, Principal did not know how much money Mutual Benefit had released until Principal received a letter dated September 17, 1991 from Howard Lowett at Unitron Graphics (A-6a).

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3. References to the Joint Appendix before the Second Circuit Court of Appeals are cited as JA-__.

B. Zucker's and Fertig's Embezzlement of $130,000 from the 401(k) Plans' Account Prior to Transfer of Any Monies to Principal

As Petitioner readily concedes, Zucker and Fertig embezzled $130,000 from the 401(k) plans' bank account before the remaining $109,811.28 released by Mutual Benefit was forwarded to Principal on October 8, 1991 to invest under the newly executed Group Annuity Contracts (A-6a).[4] The $130,000 embezzled by Zucker and Fertig was never returned by them to the 401(k) plans' account or forwarded to Principal but, as the Petitioner himself recognized, was appropriated by Zucker and Fertig for their own use (JA-15, ¶ 2). According to the sentencing memoranda submitted by Zucker and Fertig in their criminal action, they immediately used the embezzled monies in an unsuccessful effort to keep Unitron Graphics in business (JA-354, ¶ 10; 397-99, 403-08, 414-18). Having failed, Unitron Graphics filed for bankruptcy in early January 1992 (A-7a; JA-739-43).

C. Principal's Letters to Zucker and Fertig

Unaware that Zucker and Fertig had already embezzled and spent $130,000, by letter dated November 5, 1991, Principal informed Zucker and Fertig that, from "what limited recordkeeping data we have, only a portion of [the 401(k) plans'] assets" had been received (A-6a; JA-432, ¶ 14; 682). Principal further informed them that the "balance of these assets must be accounted for," and that, if Principal was to be the

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4. Principal held and invested the $109,811.28 it received in accordance with the terms of the Group Annuity Contracts (JA-431-32, ¶ 12). Today, that money either remains invested with Principal or was distributed at the request of participants in the 401(k) plans (JA-432, ¶ 12). Petitioner does not allege that Principal engaged in any improper conduct whatsoever with respect to the plan monies it held.

only investment manager, the balance of these funds should be forwarded immediately (A-6a, JA-682).

Having received no response to its November 5, 1991 letter, Principal again wrote to Zucker and Fertig on January 28, 1992, demanding that the trustees either transfer the remaining $130,000 to Principal or account for the balance of the plan assets (A-7a; JA-641-42, ¶ 3; 690-92). A few days later, a representative of Unitron Graphics advised Principal that Unitron had filed for bankruptcy and requested that Principal delay notifying the Department of Labor about the 401(k) plans' delinquency in forwarding employee deferral amounts until a buyer could be found for the business.[5] Principal refused to agree to this request (A-7a; JA-642, ¶ 5; 695).

On March 30, 1992, Principal was contacted by the Department of Labor, which was already investigating the trustees' actions regarding the 401(k) plans (JA-643, ¶ 6). Principal fully cooperated with the Department of Labor (A-8a).

D. The Department of Labor's Investigation and Subsequent Indictment of Zucker and Fertig

Although the Department of Labor began investigating Zucker and Fertig by March of 1992, it was unable to recover the already embezzled monies in the course of its investigation (A-8a).

Zucker and Fertig were subsequently indicted and pled guilty to conspiracy to embezzle funds (A-8a). Although

5. The January 28, 1992 letter also addressed Zucker's and Fertig's failure to forward new employee salary contributions to Principal in a timely fashion and demanded that these monies be forwarded within five business days (JA-690). The employee salary deferrals are not at issue in this action.

ordered to pay restitution, Zucker and Fertig were insolvent. The partial payments they later made came from loans and donations from family and friends (A-8a). The bankrupt Unitron Graphics did not have any assets with which to reimburse the 401(k) plans (A-65a; JA-761-63).

E. The Petitioner's Lack of Investigation or Evidence That Any of the Embezzled Monies Could Be Recovered

Notwithstanding discovery, his access to the Department of Labor's investigatory materials and the United States Attorney's grand jury materials, Petitioner came forward with absolutely no evidence that the $130,000 could have been recovered by any party, including Principal. Rather, as the Second Circuit noted,

> Silverman expressly declined to proffer evidence as to what Fertig and Zucker did with the funds they embezzled, or as to whether at any pertinent time they had assets that could have made good the loss. Silverman . . . evidently recognize[d] that there is no record evidence to demonstrate a causative link between Principal's inaction and the plan's loss.

(A-16a). Instead, Petitioner maintained, and still maintains, that causation simply is not an element of a claim for breach of co-fiduciary obligations, and that Principal is strictly liable for the loss caused to the 401(k) plans by Zucker's and Fertig's embezzlement (Pet. at 22).

F. The Decisions Below

By Opinion and Order dated May 16, 1996, the district court granted Principal's motion for summary judgment and denied plaintiff's cross-motion. *Silverman v. Mutual Benefit*

Life Ins. Co., No. 95-CV-0500 (ARR) (E.D.N.Y. May 16, 1996) (A-38a-67a). First, the district court found Petitioner's claim under § 405(a)(1) "unpersuasive", since there was no evidence to support his contention that Principal attempted to conceal what little it knew about Zucker's and Fertig's actions (A-55a-58a).[6] Second, the district court concluded that Petitioner could not "recover under § 405(a)(2), because Principal's conduct did not enable the trustees [Zucker and Fertig] to commit a breach [of their fiduciary duties]" (A-59a). Third, although it found that there were genuine issues of material fact as to whether Principal had sufficient knowledge of Zucker's and Fertig's breach of fiduciary duty to "trigger its duty under § 405(a)(3) to make reasonable efforts to remedy the breach," the district court concluded that "reasonable efforts could not have remedied the breach" (A-61a; 63a). Accordingly, the district court determined that Principal cannot be held liable since "the court cannot conclude that Principal's conduct caused a loss" (A-66a).

In affirming the district court, the Second Circuit summarily dismissed, as without merit, Petitioner's claims under §§ 405(a)(1) and (2) (A-15a). With respect to Petitioner's claim under § 405(a)(3), the Second Circuit ruled that

> [I]n order to satisfy the necessary element imposed by §§ 1105(a)(3) and 1109(a), Silverman must show that (i) Principal had knowledge of the

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6. The Petitioner argues at length that Principal breached its fiduciary duties by concealing information from a 401(k) plan participant (Pet. at 13-14, 21). As the district court expressly found, Principal did not conceal any information from or otherwise mislead participants (*See* discussion at A-56a-58a). The Second Circuit agreed (A-15a). Regardless, Petitioner's false accusation that Principal "purposefully secret[ed] the embezzlement" is irrelevant to whether this Court should review the Second Circuit's decision that the Petitioner had the burden of proving that the 401(k) plans' loss resulted from Principal's alleged breach of co-fiduciary duty.

> trustees' embezzlement, (ii) Principal failed to make reasonable efforts to remedy the trustees' breach and (iii) the fund's loss resulted from that failure.

(A-14a).

The Second Circuit held that Petitioner had the burden of "demonstrat[ing] in a suit for compensatory damages that the plan's losses 'result[ed] from Principal's breach of § 1105(a)(3)' " (A-13a). Because Petitioner failed to come forward with any evidence demonstrating that the plans' loss resulted from Principal's alleged inaction, as opposed to Zucker's and Fertig's embezzlement, the Second Circuit affirmed the district court's dismissal of the § 405(a)(3) claim.[7]

REASONS FOR DENYING THE WRIT

I.

THE SECOND CIRCUIT CORRECTLY APPLIED THE CLEAR STATUTORY LANGUAGE OF ERISA AND SETTLED CASE LAW

The Second Circuit properly applied the plain language of ERISA and settled law in ruling that Petitioner had the burden of proving that the 401(k) plans' losses resulted from Principal's alleged breach of co-fiduciary duty. 29 U.S.C. § 1105(a) provides:

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7. The Second Circuit did not hold that Petitioner had satisfied the first two elements under § 405(a)(3), but rather that Petitioner had adduced sufficient evidence to present a jury question on whether Principal had knowledge of Zucker's and Fertig's breach but had failed to make reasonable efforts to remedy it (A-14a). The dissenting judge was of the further view that the evidence of causation was sufficient to give rise to a material issue of fact to present to a jury, though he, too, rejected Petitioner's effort to read the causation requirement out of § 409(a) (A-15a).

> [A] fiduciary with respect to a plan shall be liable for a breach of fiduciary responsibility of another fiduciary with respect to the same plan in the following circumstances:
>
> * * *
>
> (3) if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach.

In the courts below, Petitioner argued, without citing any relevant authorities, that causation is not an element of a claim for breach of co-fiduciary obligations and that § 405(a) is essentially a "no-fault" statute.[8] Rejecting this position, the Second Circuit stated: "Like the district court, we read the relevant statutes to require Silverman to show that the loss claimed resulted from Principal's breach" (A-12a).

In recognizing the causation requirement, the lower courts looked to ERISA's exclusive civil enforcement scheme, 29 U.S.C. § 1132(a), which expressly limits the types of actions that fiduciaries can commence under ERISA when they seek recovery of compensatory damages.[9] Finding that 29 U.S.C. § 1132(a)(2)[10] was the only provision that could provide a basis

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8. Petitioner maintains that position before this Court, arguing that "29 U.S.C. § 1105 contains no 'but for' analysis" (Pet. at 22).

9. Indeed, this Court has repeatedly made clear that ERISA's carefully integrated and exclusive civil enforcement scheme, 29 U.S.C. § 1132(a), provides " 'strong evidence that Congress did *not* intend to authorize other remedies that it simply forgot to incorporate expressly.' " *Ingersoll-Rand Co. v. McClendon*, 498 U.S. 133, 144 (1990) (quoting *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 54 (1987)).

10. 29 U.S.C. § 1132(a) provides:

(Cont'd)

for the exercise of jurisdiction over Petitioner's claims for compensatory damages, the lower courts concluded that Petitioner must be seeking relief for violation of 29 U.S.C. § 1109 (A-12a; 50a).

29 U.S.C. § 1109(a), in turn, expressly requires a causal connection between the alleged breach of a duty imposed upon a fiduciary and the loss to the plan by providing that

> [a]ny person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any *losses to the plan resulting from each such breach.*

(Emphasis added) (A-13a). Accordingly, the lower courts rejected Petitioner's contention that liability for breach of co-fiduciary obligations could be imposed in the absence of a causal connection between Principal's alleged breach and the 401(k) plans' loss (A-12a-13a). As the Second Circuit explained:

> Jurisdiction for this suit for compensatory damages arises under § 1132(a)(2), which permits a fiduciary to bring a civil action "for appropriate relief under section 1109 of this title". . . . This statute therefore

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(Cont'd)

> Persons empowered to bring a civil action
>
> A civil action may be brought —
>
> . . .
>
> (2) by the Secretary [of Labor], or by a participant, beneficiary or fiduciary for appropriate relief under section 1109 of this title.

> requires a plaintiff to demonstrate in a suit for compensatory damages that the plan's losses "result[ed] from" Principal's breach of § 1105(a)(3). . . . Specifically, Silverman must show some causal link between the alleged breach of Principal's duties and the loss plaintiff seeks to recover. . . . This principle is consistent with the common law of trusts, which imposes a duty on a successor trustee to remedy the breach of a prior trustee, and imposes liability for breach of this duty "to the extent to which a loss results from [the successor trustee's] failure to take such [remedial] steps."

(A-12a-14a).

The cases are uniformly in agreement. *See Kuper v. Quantum Chemicals Corp.*, 852 F. Supp. 1389, 1396 (S.D. Ohio 1994) (" '[P]roof of a causal connection . . . is required between a breach of fiduciary duty and the loss alleged.' ") (quoting *Diduck v. Kaszycki & Sons Contractors, Inc.*, 974 F.2d 270, 279 (2d Cir. 1992)), *aff'd sub nom. Kuper v. Iovenko*, 66 F.3d 1447 (6th Cir. 1995); *Friend v. Sanwa Bank California*, 35 F.3d 466, 469 (9th Cir. 1994) (granting defendant's motion for summary judgment on the grounds that even if Sanwa had violated its fiduciary duties, the plaintiff has not presented an issue of material fact that the breach caused the losses to the plan); *Diduck*, 974 F.2d at 279 (ruling that plaintiff could not recover for breach of co-fiduciary obligations without showing that absent the breaches the monies would have been recovered); *Willett v. Blue Cross and Blue Shield*, 953 F.2d 1335, 1343 (11th Cir. 1992) (agreeing with Blue Cross' argument that causation was an element of a claim for breach of co-fiduciary duties); *Whitfield v. Lindemann*, 853 F.2d 1298, 1304 (5th Cir. 1988) (requiring a causal connection between

the breach of fiduciary duty and the loss to the plan); *Hecht v. Colorboard Packaging Corp.*, 856 F. Supp. 184, 190 (S.D.N.Y. 1994) (dismissing plaintiffs' claims for breach of fiduciary duty under ERISA on the grounds that they failed "to prove the necessary connection between the trustee's breach of fiduciary duty and actual losses incurred by the pension plan"); *Brink v. DaLesio*, 496 F. Supp. 1350, 1383 (D. Md. 1980) (ruling that imposition of liability for breach of co-fiduciary duties required proof of a causal connection between the co-fiduciary's conduct and the loss to the plan), *aff'd in part and rev'd in part on other grounds*, 667 F.2d 420 (4th Cir. 1981).

Since causation is an element of Petitioner's *prima facie* case, the Second Circuit applied the general rule that "plaintiff bears the burden of proving it" (A-16a).

> Congress has placed the burden of proving causation on the *plaintiff* by requiring him to prove that the losses "result[ed] from" the defendant's inaction. *See* 29 U.S.C. §§ 1109(a), 1105(a)(3).

(A-17a). There is nothing remarkable about this decision warranting review by this Court. In fact, the Second Circuit's decision applied centuries-old principles embedded in the common law of trusts. *See, e.g.*, George G. Bogert & George T. Bogert, *The Law of Trusts and Trustees* § 871 (2d ed. rev. 1995) ("If [the beneficiary] seeks damages, a part of his burden will be proof that the breach caused him a loss. . . . If the beneficiary makes a prima facie case, the burden of contradicting it or showing a defense will shift to the trustee.").

And, ERISA cases involving breach of co-fiduciary obligations have consistently placed the burden of proving causation on the plaintiff. For example, the Eleventh Circuit in *Willett v. Blue Cross and Blue Shield*, 953 F.2d 1335 (11th Cir.

1992), addressed, among other things, whether Blue Cross breached its co-fiduciary obligations under 29 U.S.C. § 1105(a)(3). With respect to the burden of proof, the court ruled that

> the burden of proof on the issue of causation will rest on the beneficiaries; they must establish that their claimed losses were proximately caused . . . by a failure by Blue Cross to cure May's breach.

Id. at 1343. *See Diduck*, 974 F.2d at 279 (placing the "burden of proving an amount of damages caused by the fraud" on the plaintiff); *Pension Fund-Mid Jersey Trucking Industry — Local 701 v. Omni Funding Group*, 731 F. Supp. 161, 176 (D.N.J. 1990) (rejecting plaintiff's claim that defendant breached its co-fiduciary obligations under ERISA, reasoning that "[p]laintiff has not shown any causal relationship between Southeast Bank's fiduciary duty concerning short term investments and the alleged fraudulent conduct surrounding the mortgage loans"). *See Salovarra v. Eckert*, No. 94 Civ. 3430, 1998 U.S. Dist. LEXIS 7992, at *11 (S.D.N.Y. May 26, 1998) (stating "that plaintiff's demonstration of a breach of fiduciary duty alone is not sufficient to shift the burden to defendant to disprove loss").

Here, Petitioner failed to satisfy his burden of establishing that the plans suffered a loss resulting from Principal's alleged breach of co-fiduciary duty. He merely relied on Zucker's and Fertig's embezzlement. If that were all that was needed, Petitioner could satisfy his burden of establishing a *prima facie* case simply by referring to the loss *caused by Zucker and Fertig*, without coming forward with a shred of evidence in support of the essential element of his claim *against Principal* — a causal connection between Principal's alleged failure to take reasonable steps to remedy Zucker's and Fertig's breach and the 401(k) plans' failure to recover the embezzled monies. Section 409

imposes liability for losses *resulting* from a breach, not losses *related* to a breach. Thus, the Second Circuit followed settled precedent and the plain language of ERISA in holding that Petitioner had failed to come forward with evidence that Zucker and Fertig had assets that Principal could have recovered at the time of Principal's alleged breach. As the Second Circuit found, "Silverman has come forward with no evidence bearing on when the money vanished," but instead

> expressly declined to proffer evidence as to what Fertig and Zucker did with the funds they embezzled, or as to whether at any pertinent time they had assets that could have made good the loss.

(A-19a; A-16a).

II.

THERE IS NO CONFLICT AMONG THE CIRCUITS

The Eighth Circuit's opinion in *Herman v. Mercantile Bank, N.A.*, 137 F.3d 584 (8th Cir. 1998), upon which Petitioner relies, is not in conflict with the Second Circuit's decision. In *Herman*, the Department of Labor commenced an action alleging, *inter alia*, that Timothy J. Schwent ("Schwent"), the fiduciary for a corporate health plan, breached his fiduciary duties by failing to commence an action against the corporation when it failed to pay health claims. The Eighth Circuit held that Schwent was not liable for breach of fiduciary duties because the decision not to commence an action was prudent. *Id.* at 588. Thus, the ruling in *Herman* turned upon whether the defendant had breached his fiduciary duties, not, as here, on whether a breach of co-fiduciary duty resulted in the plans' loss.

In any event, *Herman*'s discussion of plaintiff's burden is fully consistent with this case.

> We conclude that in order to prove a breach of fiduciary duty for failure to pursue any lawsuit, the Secretary must prove a lawsuit would be successful and advantage the beneficiaries of the plan. If a fiduciary won a judgment in a lawsuit against an employer but remained unable to collect on that judgment, the lawsuit would waste the resources of both the plan and the employer. *Therefore, in this case the Secretary needed to prove that if Schwent pursued a lawsuit, the health plan would have benefitted.*

Id. at 587 (emphasis added). *See id.* at 588 ("[T]he Secretary needed to prove that such suit would have succeeded and benefitted the plan participants."). The Eighth Circuit found that bringing a lawsuit would not have been prudent because "the health plan would not have won a collectable judgment." *Id.* at 587. Like the Second Circuit, the Eighth Circuit took the position that the plaintiff had the burden of proving that, had the defendant fiduciary taken action, the plan would have benefitted by recovering additional monies.

In attempting to manufacture a conflict where none exists, Petitioner relies heavily on the last paragraph before the conclusion of *Herman*, which was modified in response to the Department of Labor's request for clarification. That paragraph states, in part,

> Schwent might have presented a valid defense by meeting his burden of proving that no benefit would accrue to the plan by a successful lawsuit against [the corporation] because of [the corporation's] greatly impaired financial condition.

Id. at 588. This statement does not demonstrate a conflict, but merely reaffirms the rule in *Martin v. Feilen*, 965 F.2d 660 (8th Cir. 1992), that once the plaintiff has established that the defendant's breach of fiduciary duty caused the plan to suffer a loss, the burden shifts to the defendant to contradict plaintiff's showing or establish a defense. Indeed, in clarifying its decision, the Eighth Circuit not only reaffirmed that it was the Secretary's burden to prove that a lawsuit would have benefitted the plan participants, but it also rejected the Secretary's invitation to distinguish its decision from *Silverman* or even note any disagreement with the Second Circuit's decision (*Cf.* Pet. at 25).

And, as the Second Circuit found, *Martin* is fully consistent with this case. *Martin* involved *calculation of damages* after plaintiff proved a loss to the plan resulting from the defendant's breach of fiduciary duty, not whether the plaintiff had satisfied its threshold burden of showing that the breach caused a loss. The Second Circuit explained:

> the issue in Martin involved the calculation of damages after the plaintiff proved a prima facie case that the plan suffered a loss resulting from the defendant's breach of its fiduciary duty. See *id.* (holding that Secretary of Labor had established a prima facie case by proving that defendants "violated § 1104 by causing the ESOP to engage in stock transactions that caused specific injury to the ESOP at the time in question."

(A-17a) (emphasis in original).

Petitioner also errs in arguing that the Second Circuit's approach is somehow at variance with *Kemmerer v. ICI Americas Inc.*, 70 F.3d 281 (3d Cir. 1995) (Pet. at 27). There, the Third

Circuit rejected the "appellants' contention that the burden [of proof] should shift simply because this is an ERISA case." *Id.* at 290. Reaching this conclusion, the court explained:

> To be sure, in certain ERISA cases, courts have placed the burden of proof on the trustee of the plan. But those cases involved first, the trustee's breach of fiduciary duty, and second, a definite loss. . . . Neither of the prerequisites to burden-shifting is present here.

Id.

Nor does *Roth v. Sawyer-Cleator Lumber Co.*, 16 F.3d 915 (8th Cir. 1994), help Petitioner in creating a conflict where none exists. The Eighth Circuit there reversed the district court's grant of summary judgment to the defendant fiduciaries, finding that there were questions of fact concerning whether the fiduciaries' investment decisions were prudent. In discussing the plaintiffs' burden, the court again simply reiterated the rule in *Martin v. Feilen*, 965 F.2d 660 (8th Cir. 1992), which is not in conflict with the Second Circuit's decision here.

McDonald v. Provident Indemnity Life Insurance Co., 60 F.3d 234 (5th Cir. 1995), is also consistent with the case at bar. In *McDonald*, the court ruled that recovery was barred because the failure of a fiduciary to inform an employer of a schedule for re-rating premiums did not result in a loss to the plan, but only to the individual plan participant who was bringing suit. In passing, the court stated that the plaintiff has the burden of proving a breach of fiduciary duty and a loss to the plan. *Id.* at 237.

In short, just as the Eleventh Circuit in *Willett*, the Second Circuit correctly placed the burden on Petitioner to demonstrate

that Principal's alleged breach of co-fiduciary duty caused a loss to the 401(k) plans. That decision is not in conflict with the decisions of other circuit courts, and not a single court has suggested there is any such conflict. Rather, the Second Circuit's decision simply applies the basic rule that the plaintiff has the burden of proof with respect to the elements of his claim for relief.

III.

MOREOVER, THIS ACTION INVOLVES A UNIQUE SET OF FACTS INVOLVING AN ALLEGED BREACH OF CO-FIDUCIARY DUTY AND IS NOT AN APPROPRIATE CASE FOR ADOPTING A BROAD RULE OF LAW SHIFTING THE BURDEN OF PROOF TO INVESTMENT MANAGERS

This action involves an alleged breach of co-fiduciary, not fiduciary, obligations. There are no allegations that Principal engaged in any self-dealing, prohibited transactions or commingling of funds, or that it received any benefit as a result of Zucker's and Fertig's embezzlement. Further, Principal did not actively participate in their breach or otherwise create obstacles to Petitioner's ability to prove that Principal's alleged action or inaction — as opposed to Zucker's and Fertig's actions — caused a loss to the 401(k) plans. Indeed, if there were any evidence that Principal could have remedied the 401(k) plans' loss, which there is not, Petitioner could easily have obtained that evidence from the Department of Labor, the United States Attorney or through discovery or investigation of Zucker's, Fertig's and Unitron Graphic's financial condition.

To the extent that existing authorities can be read to impose a burden on a defendant fiduciary to disprove causation, those cases involved factual situations vastly different from that

presented here. First, none involves alleged breaches of co-fiduciary, as opposed to fiduciary, duties. Second, the fiduciary duty cases shifting the burden involve (a) calculating damages after liability has been established or (b) a fiduciary's commingling of funds, self-dealing, active misconduct or creation of obstacles to the plaintiff's ability to prove the amount of damages. *See The New York State Teamsters Council Health and Hosp. Fund v. Estate of DePerno*, 18 F.3d 179 (2d Cir. 1994) (shifting the burden to defendant to prove damages in an action involving prohibited transactions)[11]; *Leigh v. Engle*, 727 F.2d 113, 138-39 (7th Cir. 1984) (imposing the burden of proving the amount of damages on the defendants, where defendants have "made it difficult to disentangle commingled profits"); *Donovan v. Bierwirth*, 754 F.2d 1049, 1052 (2d Cir. 1985) (placing burden of proving damages on defendants, whose active misconduct in breaching their fiduciary duties made it difficult, if not impossible, for plaintiffs to prove their damages); *Martin v. Feilen*, 965 F.2d 660 (8th Cir. 1992) (shifting the burden for purposes of calculating damages only after the plaintiff established that the defendants' self-dealing and conflict of interest caused a loss to the plan); *Ned v. United Mine Workers of America*, 556 F.2d 190, 210 (3d Cir. 1977) (shifting the burden to prove, as a matter of defense, that the loss would have occurred in the absence of a breach only *after* plaintiffs proved that they suffered a loss as a result of defendants' breach of their fiduciary duties).[12]

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11. In *Salovarra v. Eckert*, No. 94 Civ. 3430, 1998 U.S. Dist. LEXIS 7992 (S.D.N.Y. May 26, 1998), the district court found that *DePerno* did not support finding that once the plaintiff demonstrated a breach of fiduciary duty, the burden shifted to the defendant to disprove a loss and a causal connection between a breach and a loss. The court explained, "[i]n *DePerno*, plaintiffs clearly established both a breach and loss to the fund . . . before the burden shifted to defendants." *Id.* at *11.

12. In *United States Life Insurance Co. v. Mechanics & Farmers Bank*, 685 F.2d 887, 896 (4th Cir. 1982), the court rejected plaintiff's

(Cont'd)

None of the rationales for shifting the burden applies to Petitioner's claims against Principal. Rather, to shift the burden in an action for breach of co-fiduciary obligations under the facts presented here would make investment managers, such as Principal, virtual insurers of the misdeeds of the named fiduciaries and trustees of a plan. Investment managers would be presumptively liable for the entire amount of a plan's loss simply by learning of an earlier breach that caused the loss. The investment manager would be presumptively liable even if, as here, it had no role in causing the loss. Imposition of such broad ranging liability for breach of co-fiduciary obligations finds no support in the law and would serve only to burden beneficiaries with additional fees that investment managers would be forced to charge to cover their risk of being held liable for losses caused by other fiduciaries and over which they had no control.

(Cont'd)

> novel proposition that, whenever a breach of the obligation by a trustee has been proved, the burden shifts to the trustee to establish that any loss suffered by the beneficiaries of the trust was not proximately due to the default of the trustee, and that, unless the trustee meets this burden, recovery against the trustee for the full loss follows in course.

Reaching this conclusion, the court distinguished cases which shifted the burden on the grounds that they involved "the 'rule of trust pursuit' or the situation where a trustee has converted trust property and commingled the proceeds with his own funds." *Id.* In this situation, if "the beneficiaries are prevented from separating their assets from the 'entire mass' in which their assets are commingled," equity will place the burden of proving what portion of the assets do not belong to the trust on the breaching trustee. *Id.*

CONCLUSION

For the reasons stated, the Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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APPENDIX

APPENDIX A — RELEVANT STATUTES INVOLVED

29 U.S.C. § 1105. Liability for breach by co-fiduciary

(a) Circumstances giving rise to liability

In addition to any liability which he may have under any other provisions of this part, a fiduciary with respect to a plan shall be liable for a breach of fiduciary responsibility of another fiduciary with respect to the same plan in the following circumstances:

(1) if he participates knowingly in, or knowingly undertakes to conceal, an act or omission of such other fiduciary, knowing such act or omission is a breach;

(2) if, by his failure to comply with section 1104(a)(1) of this title in the administration of his specific responsibilities which give rise to his status as a fiduciary, he has enabled such other fiduciary to commit a breach; or

(3) if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach.

Appendix A

29 U.S.C. § 1109. Liability for breach of fiduciary duty

(a) Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary. A fiduciary may also be removed for a violation of section 1111 of this title.

(b) No fiduciary shall be liable with respect to a breach of fiduciary duty under this subchapter if such breach was committed before he became a fiduciary or after he ceased to be a fiduciary.

29 U.S.C. § 1132. Civil enforcement

(a) Persons empowered to bring a civil action.

A civil action may be brought —

(1) by a participant or beneficiary —

(A) for the relief provided for in subsection (c) of this section, or

(B) to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan;

(2) by the Secretary, or by a participant, beneficiary or fiduciary for appropriate relief under section 1109 of this title;

(3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this subchapter or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of this subchapter or the terms of the plan;

(4) by the Secretary, or by a participant, or beneficiary for appropriate relief in the case of a violation of 1025(c) of this title;

(5) except as otherwise provided in subsection (b) of this section, by the Secretary (A) to enjoin any act or practice which violates any provision of this subchapter, or (B) to obtain other appropriate equitable relief (i) to redress such violation or (ii) to enforce any provision of this subchapter;

(6) by the Secretary to collect any civil penalty under paragraph (2), (4), (5), or (6) of subsection (c) or under subsection (i) or (*l*);

(7) by a State to enforce compliance with a qualified medical child support order (as defined in section 1169(a)(2)(A) of this title);

(8) by the Secretary, or by an employer or other person referred to in section 1021(f)(1) of this title, (A) to enjoin any act or practice which violates subsection (f) of section 1021 of this title, or (B) to obtain appropriate equitable relief (i) to redress such violation or (ii) to enforce such subsection; or

(9) in the event that the purchase of an insurance contract or insurance annuity in connection with termination of an individual's status as a participant covered under a pension plan

with respect to all or any portion of the participant's pension benefit under such plan constitutes a violation of part 4 of this title[1] or the terms of the plan, by the Secretary, by any individual who was a participant or beneficiary at the time of the alleged violation, or by a fiduciary, to obtain appropriate relief, including the posting of security if necessary, to assure receipt by the participant or beneficiary of the amounts provided or to be provided by such insurance contract or annuity, plus reasonable prejudgment interest on such amounts.

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1. So in original. Probably should be "subtitle".